

The Economist

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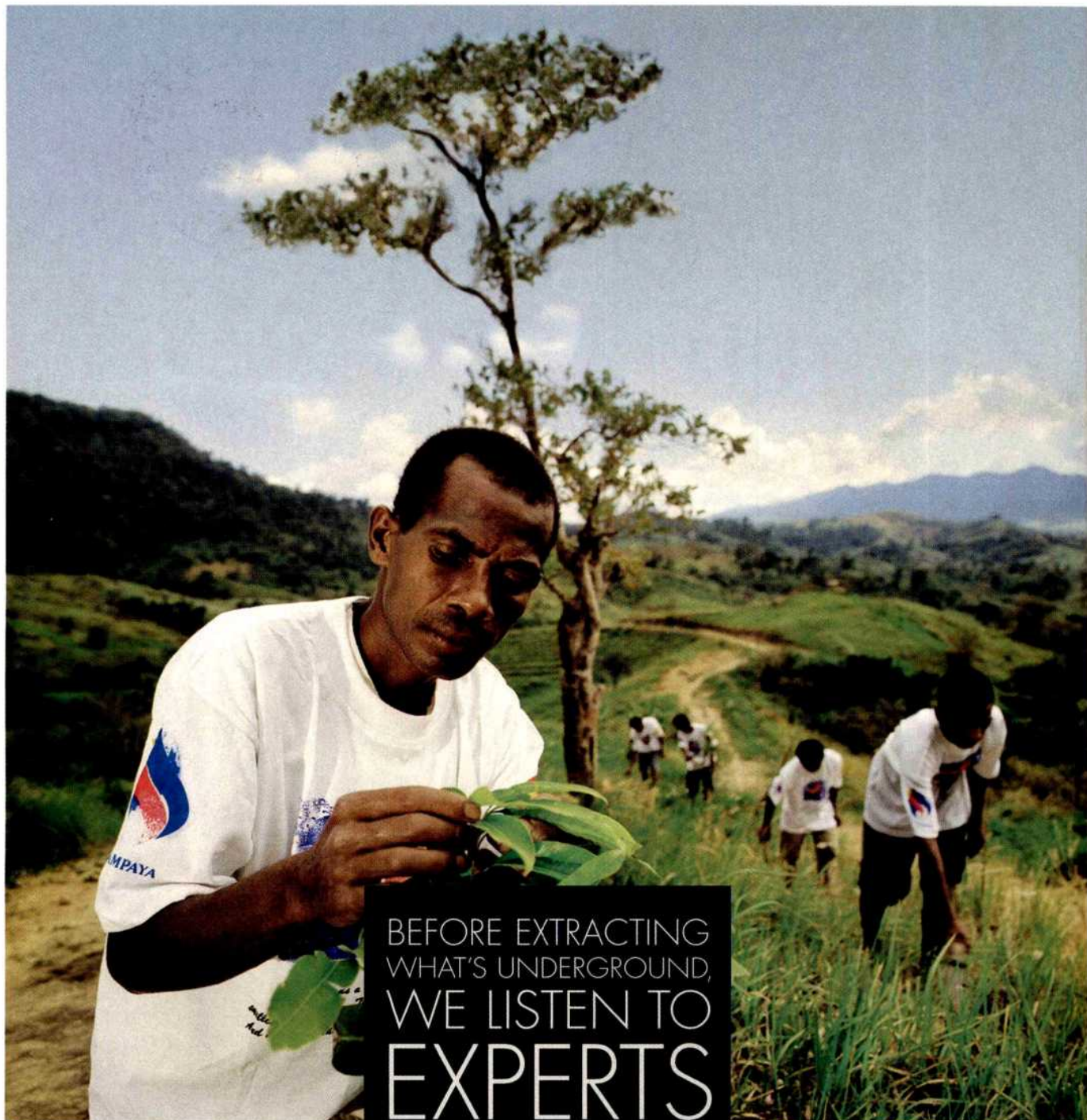
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A tale of two bellies

The remarkable demographic difference between America and Europe



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On the cover
The population of the United States is growing strongly, with rising fertility rates and rapid immigration, and could even reach 550m by 2050. The population of Western Europe is ageing and will soon start to fall. These trends could have big implications: leader, page 9. The demographic details, pages 18-20

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Politics



Two of Europe's biggest rivers, the **Elbe** and the **Danube**, flooded towns and villages in Germany, the Czech Republic and, less extensively, Hungary, whose capital, Budapest, managed to stay above the waves. Dresden, the capital of the German state of Saxony, did not escape. Across the region, more than 100 people died and hundreds of thousands were forced out of their homes. Repairs in Germany, the worst hit, may cost €15 billion (\$15 billion).

A report commissioned by **Germany's** government and chaired by a Volkswagen director, Peter Hartz, proposed labour-market reforms that included ways to create more temporary and part-time jobs and to make it harder to get the dole. Chancellor Gerhard Schröder endorsed the report's suggestions. Pre-election grandstanding and panic measures, declared the conservative opposition.

Five members of a previously unknown Iraqi opposition group seized the **Iraqi embassy in Berlin**, calling for Saddam Hussein's overthrow. German commandos removed them without bloodshed after five hours.

A lethal week in **Russia**: at least 115 Russian soldiers were killed when a military helicopter was shot down in the disaffected Russian republic of Chechnya; a gas explosion killed at least eight people in a block of flats in Moscow; and a member of the Duma, Vladimir Golovlev, was shot dead by assailants unknown.

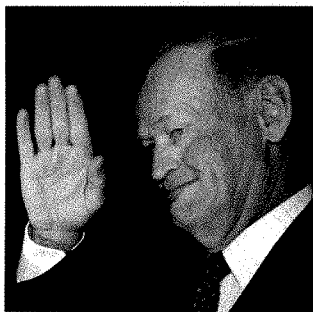
After one of **Britain's** biggest police searches, the bodies of two ten-year-old girls missing for 17 days from their homes in Soham, Cambridgeshire, were discovered in a nearby wood. A local school caretaker was charged with their murder; his partner faced charges related to the killing.

Cut down in their primary Two controversial members of the House of Representatives lost their **primary races** in Georgia. Bob Barr, a critic of gun control, lost to another right-wing Republican. One black Democrat, Cynthia McKinney, a supporter of Arab causes, was beaten by another, Denise Majette, who attracted support from Jews around the country.

President George Bush summoned **senior security advisers** to a meeting in Texas. The White House insisted it was to discuss the transformation of the Defence Department, not an attack on Iraq. At a press conference, he said he was a patient man who would look at all options and consult widely before deciding how to change the regime in Iraq.

Two critical reports examining the way the New York fire and police departments acted on **September 11th** were released. They prompted pledges from the emergency services to improve their command procedures and communication.

Chrétien's adieu



Jean Chrétien, prime minister of **Canada**, said that he would step down in February 2004. His leadership of the Liberal party faced a powerful challenge from Paul Martin, his former finance minister.

Argentina's government sent a draft letter of intent to the IMF and said that it hoped for a speedy but limited agreement to roll over its debts to the Fund itself. But the country's Congress approved two bills which partially reverse the repeal, demanded by the IMF, of a debtor-friendly bankruptcy law.

In meetings with President Fernando Henrique Cardoso, opposition candidates who head the opinion polls for **Brazil's** presidential election were guarded about endorsing a recent IMF agreement. But they repeated their commitment to responsible macroeconomic policies in 2003. Brazil's currency and bonds had a stronger week.

China crisis

A state of emergency was declared in central **China** as the country's second-largest freshwater lake threatened to overflow, endangering up to 10m people. In the south, flash floods and landslides have killed 100 people in the past two weeks.

The United Nations began an investigation into allegations that up to 1,000 captured Taliban soldiers ended up in mass graves near Mazar-i-Sharif, in **Afghanistan**. The men are said to have died last November after being packed into sealed cargo containers by Northern Alliance soldiers for transportation to prison.

Pakistan's president, General Pervez Musharraf, outlined sweeping constitutional changes giving him the right to dismiss an elected government and choose the heads of the armed services. He said that he would stay on as president for five years. General Musharraf maintained that the changes would strengthen democracy; critics claimed that they would strengthen his own grip on power.

Officials overseeing next month's vote for a new legislature in Indian-administered **Kashmir** asked for a change of personnel to ensure free

and fair elections. Pakistan says a referendum should first be held to allow Kashmiris to choose between rule by India or Pakistan, or independence.

Muslim guerrillas in the southern **Philippines** beheaded two Christian preachers.

Genocidal? Not me

Augustin Bizimungu, a former head of Rwanda's army who is charged with being one of the chief architects of the 1994 genocide that killed 800,000 people, pleaded not guilty at the international tribunal in Arusha.

Abu Nidal, a notorious Palestinian terrorist who was responsible for the murder of hundreds, died in Baghdad. The Iraqis say he committed suicide.

Israel's security forces arrested several members of a **Hamas cell** in East Jerusalem which, they claim, was responsible for the bombing of the Hebrew University.



Zambia, though facing famine, said it would accept food aid only if it contains no genetically modified product. Much of the food provided by the World Food Programme to the region comes from American farms, where modified grain is common.

An Islamic appeal court in **Nigeria** upheld a sentence of death by stoning for adultery against a woman who was found guilty after bearing a child outside marriage.

The trial started in **Mozambique** of four railway workers accused of causing a train crash that killed 195 people. ►►

Business

Michael Kopper, right-hand man to Andrew Fastow, **Enron's** chief financial officer, pleaded guilty to charges of fraud and money laundering. He is the first insider to admit to a criminal role in connection with the collapse of the energy giant and his testimony may be used against former colleagues, including Mr Fastow, increasing the chances of further successful prosecutions.

Entertainment news

AOL Time Warner agreed to pay \$3.6 billion and give a stake in a new cable company to **AT&T** to unwind a partnership in Time Warner Entertainment. AT&T will exchange its 27.6% of TWE for cash and shares, and 21% of a cable subsidiary that AOL eventually plan to spin off.

Vivendi Universal's woeful results and crashing shares prompted Jean-René Fourtou, the embattled media company's chief executive, to send a letter to employees and shareholders reassuring them that he could put things right, although without really specifying how. Vivendi was also near to selling its 50% stake in Vizzavi, an Internet portal, to its partner in the joint venture, Vodafone, for some €150m (\$147m).

Sir Martin Sorrell, boss of **WPP**, was pessimistic about the prospects for the world advertising industry after announcing poor results at the advertising giant. Pre-tax profits fell by 17% in the first half compared with a year ago, to £210m (\$303m); Mr Sorrell thinks that the world advertising slump may persist until 2004.

Still flying

As American airlines continue to languish, airlines elsewhere fared better. **Qantas** announced a 3% increase in profit for the year to the end of June compared with the previous 12 months to A\$428m (\$224m), partly aided by the

demise of Ansett, its domestic rival, last year. It also announced a rights issue to raise A\$800m; British Airways said that it would not participate. So BA's stake in the Australian airline will decrease from 21% to 17%.

Lufthansa beat expectations with an operating profit of €332m (\$298m) in the first half after cutting costs and capacity in the wake of September 11th. In recent weeks both KLM Royal Dutch and British Airways have announced profits in the past quarter.

Qwest for cash

Qwest Communications, an American telecoms company, made inroads into its debt-pile of over \$26 billion with the sale of its directory-publishing business, QwestDex, for \$7.1 billion, to two American private-equity firms, Carlyle Group and Welsh, Carson, Anderson & Stowe. The deal could save Qwest from bankruptcy—for the moment.

KPN lost €9.3 billion (\$8.5 billion) in the second quarter after the Dutch telephone company wrote off some €9 billion, mainly reflecting the plunging value of investments in third-generation mobile services outside its home market.

Deutsche Telekom revealed losses of €3.9 billion (\$3.5 billion) in the first half but its hefty debts fell. The German telecom's company was also said to be considering a full or partial sale of VoiceStream, its American mobile business, to raise more cash.

Home improvements

Profits at **Home Depot**, America's largest home-improvement retailer, rose by 28% in the second quarter over a year ago to \$1.2 billion as Americans continued to upgrade their homes. **Lowe's**, number two in the sector, announced a 42% increase in profits in the quarter to \$467m.

Axa sharpening

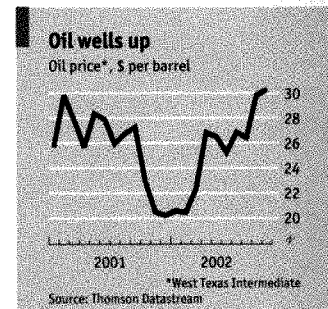
Axa, recently forced to defend its share price publicly, published results bettering expectations for the first half despite high insurance claims and weak financial markets. The European insurance giant saw operating profits increase by 17% to €1 billion (\$915m) putting on track to meet its target of increasing profits by one fifth for the year.

South Korea's government selected **Hana Bank** to take over **Seoulbank**, a state-owned rival, for an estimated 1.1 trillion won (\$923m) in shares, turn-

ing down a similar cash offer from Lone Star, an American private-equity company.

The **FSA**, Britain's financial-services regulator, ruled out restrictions on short-selling by hedge funds. Some investors have blamed shorting by the funds for recent volatility in stockmarkets. The financial-services watchdog also published a paper that considers ways to open hedge funds to retail investors.

Crude data



Oil rose above \$30 a barrel for the first time in 18 months as talk spread of an American attack on Iraq and fears grew of a shortage of stocks. New figures revealing higher-than-expected stocks in America cooled things, for the time being at least.

Other economic data and news can be found on pages 72-74





 **Busan**

 **Kuwait**

Beijing Seoul
Shanghai
Chengdu
Kunming
Guangzhou
Vientiane
Chiang Mai
Kolkata
Kathmandu
Dhaka
Lahore
Delhi
Dubai
Muscat
Karachi
Mumbai
Colombo
Yangon
Tokyo
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A tale of two bellies

The remarkable demographic difference between America and Europe



DEMOGRAPHY, said Auguste Comte, a 19th-century French philosopher, is destiny. Well, not exactly, is the correct reply, for other things matter too and even demographic trends can change over the decades. But it is certainly

important, and its effects endure for longer, and have a wider impact, than most other social or economic forces. More attention should be paid to population trends, by politicians, economists, sociologists and even those studying international relations. For something extraordinary is happening, right now, in the populations of the United States and of Western Europe.

More strictly, the extraordinary change is taking place just in the United States. But if it continues, it will open up a remarkable gap between the rich countries on the opposite sides of the Atlantic, which could have big policy implications for both of them. At present, West European countries are following what seems to be a normal demographic path: as they became richer after the 1950s, so their fertility rates fell sharply. The average number of children borne by each woman during her lifetime fell from well above the "replacement rate" of 2.1—the rate at which the population remains stable—to less than 1.4 now. The United States followed that pattern too, until the 1980s. But then something astonishing happened: the American fertility rate reversed its decline, and even rose quite sharply, back almost to the replacement rate.

During the 1980s and 1990s, both America and Europe also admitted a lot of immigrants. But while Europe's immigration was enough merely to keep its population roughly stable, the combination of immigration and rising fertility—among native-born Americans as well as recent immigrants—meant that America's population actually grew, at rates exceeding most expectations. As our special report on pages 18-20 shows, if, as demographers now expect, America's higher fertility rates persist and even rise further, then during the next quarter century that country's population will rise from 281m now to 350m-400m, and by 2050 could be anywhere between 400m and 550m. Western Europe's population, meanwhile, will probably be falling.

The elixir of youth

So what? A bigger population will bring lots of problems, ranging from urban sprawl to costlier education, even, perhaps, new social tensions. Europe's much-vaunted advantage in the "quality of life" of its citizens could, on that theory, merely be enhanced by these trends. And a large population is not, on its own, a route to riches or to power, whether military or economic. If it were, India and China would long since have been the world's most powerful countries.

Yet America's demographic exceptionalism does not merely rely on raw numbers. It relies, rather, on the nature of the population growth, and what that growth will do to its demographic structure. If the rising fertility rate among native-born Americans persists, it will mean that the growth is

steady—there will be no sudden addition of a huge pool of poor, as occurred with German unification—and a bit more balanced ethnically than was previously assumed. The most important aspect, though, can be summed up in one word: youth. While Europe's population will, on average, be ageing, America's will stay much younger. That will increase the burden of education spending, but reduce the burden of pensions and health care for the elderly, especially towards the middle of the century. A younger population is likely to mean lower labour costs (as it did, for example, for Japan during the 1960s and 1970s, when its workforce was younger than America's) and, most likely, a more entrepreneurial culture.

In other words, you ain't seen nothing yet. These trends suggest that anyone who assumes the United States is now at the zenith of its economic or political power is making a big mistake. There are plenty of other ways in which America could weaken itself economically or politically, but demography will offer a fine basis for future growth, and strength. The United States could well become even more powerful than it is today even if—as is to be hoped—populous developing countries such as India and China also manage to get richer. Demography will, though, define the domestic political agenda in America, raising the importance still further of education and urban sprawl, and forcing both parties to try even harder to capture the hearts of Latino voters.

Older, wiser but weaker

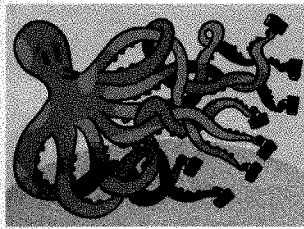
Demography should set Europe's agenda, too. Europeans already know that their societies are ageing, and that they have to find ways to ease pension and health burdens. What these demographic trends also suggest, however, is that enlargement of the European Union to take in the poorer countries of Central and Eastern Europe is even more urgent than was previously thought. It will not make Europe younger, for the eastern countries' populations are also ageing, but it will bring some new entrepreneurial spark, especially if Turkey's application is taken seriously and especially if migration from the newcomers (and from elsewhere) into Western Europe is encouraged. If Europeans do not care about their position relative to America, then perhaps this should not matter. But all the talk, at least among politicians, of uniting to strengthen Europe's voice in the world, suggests that they do.

Enlargement alone will not be enough. If little else is done, the West Europeans will retain their fiscal burdens and rigid economies (see page 52) and watch admiringly (or sadly) as the real growth takes place to their east—or else, as seems all too possible, they will hamper that growth by forcing the newcomers to share their own restrictions and subsidies. Instead, Western Europe needs to bring the new sparkiness right into its midst, both by becoming more open to immigration and by encouraging more entrepreneurial vigour among existing citizens. It is not a case of having to copy American ways. It is a case of returning to the European ways that in the 1960s brought rapid economic growth—before public spending climbed, welfare states spread and regulations multiplied. History can help destinies, too. ■

Banking strategy

Thanks a bundle

The model of a vast, integrated financial firm is fast going out of favour



AMONG executives, it is not just Sandy Weill and his lieutenants at Citigroup who are alarmed at the \$80 billion drop this year in the shares of the world's biggest financial institution. Until recently, Citigroup was also the most admired bank

in the world. Executives at many lesser banks have set their course by Citi, the very model of a diversified financial-services group. The bank seemed to have everything: size, allowing economies of scale and a world reach; skill at integrating commercial with investment banking, should corporate customers demand both credit and advice; and fund-management and insurance channels, through which investment-banking products could be pumped, sorry, cross-sold. What is more, Citigroup seemed to make money. Yet if investors are now so savagely marking the Citigroup model down, what does that imply for the Citi-mimicking strategies of Deutsche Bank, UBS, J.P. Morgan Chase and others who hoped to use balance-sheet size to muscle into investment banking?

Fads come and fads go—heaven knows, not least among investors. It is possible that this share-price fall will prove a summer storm, of little consequence. More likely, though, it points to two profound, if tardy, discoveries about the integrated model of financial services.

First, that perhaps it was not such a bright idea to offer credit to investment-banking clients at less-than-market rates—even though this has been a chief calling card over the past few years for those commercial banks that wanted to get into the juicy business of investment banking. After all, it is precisely the riskiest borrowers, those who have trouble bor-

rowing elsewhere, that are most likely to take up aspiring investment banks on their offers of credit. This is painfully obvious now that banks have the debt of seriously weakened or even bankrupt companies on their books.

Reputations are golden

Mr Weill, his defenders say, was canny enough largely to avoid this pitfall at Citigroup, which appreciated better than most the riskiness of its borrowers. Maybe so. But that leads directly to the second, more profound discovery. Citigroup knew that Enron, to which it was a big lender, carried risks. To counter the risks, the bank structured loans to the energy-trading giant in ways that were at once opaque and designed to ensure Citi stood at the head of the creditors' queue, should Enron ever run into trouble. Illegal or just too-clever-by-half?

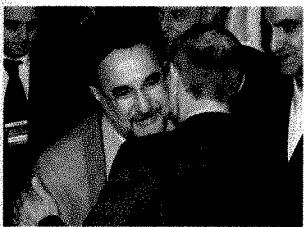
Either way, Citigroup now has a problem of reputation. What once were presented as wonderful synergies now look like giant conflicts of interest. Size and complexity are no longer seen as virtues by customers, for the bigger you are, the more likely reputational shocks will come from unexpected quarters. Citigroup's reputation is also suffering elsewhere, notably from regulatory investigations into boom-time public offerings, and into the conflicted role of analysts such as Jack Grubman, a telecoms expert who quit Citi last week, pocketing \$32m. Mr Grubman both advised investors and sat in on board meetings at WorldCom, now bust but once a client.

Conglomeration is being discredited astoundingly soon after America's Gramm-Leach-Bliley act pulled down the last 1930s restrictions on financial conglomerates in 2000. A mistake? Not necessarily. This time it will be markets and customers who will vote for clearer, less conflicted sources of advice, credit and investment. Let the unbundling begin. ■

Russia and its friends

Blowing your chances

Vladimir Putin's dealings with Iraq and Iran risk alienating his new friends in America



IF YOU can judge a friend by the company he keeps, what does that say about the new friendship George Bush thought he had with Russia's Vladimir Putin? The Russian president's decision, after the September 11th attacks, to line his country

up alongside America in the fight against terrorism seemed to mark more than an end to the long post-Soviet sulk about lost influence. He seemed to grasp, as others had failed to, that Russia's standing in the world will depend on the strength of its economy, not the tally of its missiles; and on how it helps tackle new threats, including terrorism and the spread of weapons of mass destruction, not on the mischief it can make.

But Mr Putin's clear vision, which worryingly few of his diplomats and generals seemed to share, is going cloudy again.

Russia is to sign a new multi-billion-dollar trade agreement with sanctions-hobbled Iraq, despite that country's defiance of UN disarmament resolutions. And not only does Mr Putin insist on completing the controversial Bushehr nuclear power reactor in Iran—though its regime barely disguises its ambition to build a nuclear bomb—his government is now offering to build several more such reactors. Since both Iraq and Iran have long cheated on their proliferation promises, and are both founder members of Mr Bush's "axis of evil", all this seems calculated to offend. But it is not just Mr Putin's next invitation to Mr Bush's Texas ranch that is at stake. He risks damaging Russia's own interests as well.

Of course, even friends can disagree. Mr Bush's good-ver- ➤

► sus-axis-of-evil rhetoric grates on plenty of European nerves too. It makes sense for Russia to want to be on as good terms as possible with the neighbours. Iran in particular has influence in Russia's Islamic reaches, which, as this week's military casualties in Chechnya show, Mr Putin is still struggling to subdue. Moreover he insists that he is no proliferator. Yet Russia's record suggests otherwise: its firms have done more than most (aside from North Korea and China), sometimes with official connivance, to help others acquire longer-range missiles and nuclear, chemical and biological weapons.

Seen in this light, the new framework deal with Iraq looks custom-made for sanctions-busting. Russia denies this. It wants to get back the billions Iraq owes it, and, like France and others, position itself for new oil contracts when sanctions are eased. When it seemed that Iraq would wriggle out of both UN sanctions and weapons inspections, Russia defended it in the Security Council, hoping to be first in line for new business. When Mr Putin later co-operated with Mr Bush in devising "smarter" sanctions, Russia left no doubt that it still expected its commercial interests to be respected, whoever runs Iraq. The new agreement may be just another marker; its \$40 billion figure for trade benefits is likely to prove vastly inflated.

Similarly, the proposals to build a clutch of new reactors for Iran are just proposals. Yet America and Russia had been groping towards a compromise over Bushehr. Russia has said it

will manage the fuel for the reactor, preventing Iran from extracting its bomb-usable plutonium, and will press Iran to sign up to stringent new international inspections, making cheating harder. Just as it looked as if further damage to relations could be avoided, Russia has multiplied that risk. As Mr Putin ought to know, and as India's bomb programme proved, just about any civilian nuclear expertise can be useful to a determined weapons builder. So why give more?

Why Russia does it

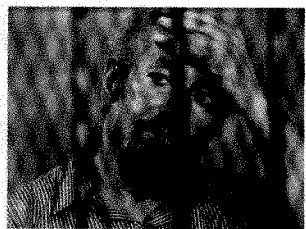
The main motive is cash. To an economy that still bumps along selling mostly weapons, oil and gas, more reactors for Iran means more money coming in. That said, some Russian officials—still convinced that anything that annoys America must benefit Russia—will be only too happy to advise stepping hard on Mr Bush's toes.

Yet the missile and nuclear expertise Russia sells today could well be a threat to its own security tomorrow. In any case America and Europe, not Baghdad and Tehran, are the places where Mr Putin needs to look for trade and investment on a big enough scale to finance Russia's recovery. He now sits at the G8 top table and helped inaugurate a new NATO-Russia council. He has given Russia a chance to be accepted as a reliable partner by the West, not shunned as a trouble-maker. But he can still blow it. ■

America and the Arab world

Slapping Egypt's wrist

The United States is right to demand more than oil and stability from its friends in the Middle East



FOREIGN aid, when not strictly humanitarian, is a political instrument, to be given or withheld for reasons of enlightened self-interest. America, having failed by other means to persuade Egypt to reconsider the unjust punishment of an

American citizen, has said it will not be giving the Egyptians some extra money they had asked for. A generous price for a man, perhaps, but perfectly proper. But is this all it was? It could, perhaps, turn out to be the start of something important: America using aid and influence to encourage an opening up of the closed Arab world.

The Egyptians had asked for the money simply because Israel had been promised an extra \$200m for "counter-terrorism" and American aid to the two countries, since their 1978 peace deal, is doled out on a three-to-two ratio. (Their yearly hand-outs are being very slowly phased out, but they still get close to \$3 billion and \$2 billion each, about one-third of America's foreign aid.) However it was unlikely that Egypt would ever have got the extra \$134m; the House Appropriations Committee had already turned it down, and even the Israeli supplement has been temporarily swept away in a dispute over the budget. Nevertheless, George Bush went out of his way to tell Hosni Mubarak that since he had locked up Saadeddin Ibrahim, he should not expect any extra titbits.

Mr Ibrahim, a social scientist at the American University of Cairo with dual Egyptian-American citizenship, is well

known at home and abroad. After a retrial, he was sentenced to seven years in prison on various charges, but mainly because he was said to have tarnished Egypt's image abroad. Saying publicly what a lot of Egyptians say privately, he spoke out against the repressiveness of the regime and the tawdriness of its elections. That so prominent a man was picked for punishment highlights the message Mr Mubarak was sending: however non-threatening your dissent, and however well-connected you may be, you had still better shut up.

What message is Mr Bush sending back? If it is a limited slap on the wrist, the affair could fade into being no more than a blip in the relations between two countries that need each other, even if they don't much like each other. But it could evolve into a much wider message, signalling a switch in America's traditional priorities.

Mr Bush's Arab world

Until now, the United States has chosen its Arab friends for their stability, their anti-radicalism, their oil, and their non-belligerence towards Israel. The fact that most of them have a dismal record on human rights, and are exceedingly reluctant to hold genuine elections (or indeed any elections at all) has weighed light in the balance. The rulers are safely pro-American, and the populations can, more or less, be kept quiet.

If America were a country like any other, its friends should be its own business, whatever their anti-social habits. But Mr Bush is ambitious. He intends to bring about the overthrow of the Iraqi regime, and he hopes for a just Israeli-Palestinian peace. Moreover, he speaks of these things happening in the ►►

► context of a visionary Arab world in which freedom, tolerance and moderation reign.

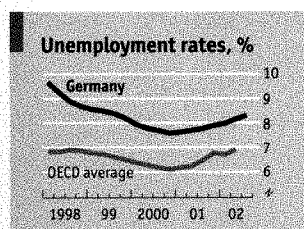
It is a lovely vision, and one that many of his Arab listeners share. But it jars with an American policy that has actively supported useful regimes without questioning whether they fit into that vision. No American voices have been raised at the way Egypt and some others bundle into jail elderly gentlemen who are as harmless and possibly as learned as Mr Ibrahim but happen to be convinced Islamists. And there is positive American encouragement for excessively nasty Arab habits when it comes to interrogating al-Qaeda suspects.

Yet, perhaps, this policy is now in the process of being rethought. Political America has recently been giving voice to its reservations about undemocratic Saudi Arabia, and the Saudis have been responding angrily (see page 33). Holding back aid to Egypt is an excellent sign, albeit symbolic. Next month, or so it is suggested, the administration may launch a programme for spending some of its dollars on Arab public institutions and public debate. What else? Well, one step is obvious to everybody bar the United States itself: put sensible conditions, such as a freeze on Jewish settlement of the occupied territories, on some of that lavish aid to Israel. ■

Germany's labour-market reforms

Too little too late, Mr Schröder

Germany's economy has long needed radical treatment, not tinkering



YOU can hardly blame Germany's voters, a mere month before a general election which the chancellor is predicted by most pollsters to lose, for a cynical smirk at his endorsement of a belated plan to slash his country's woefully high rate of unemployment, the very issue that is most likely to spike his chances of re-election. Two years ago Gerhard Schröder promised to cut the number of Germans without jobs to less than 3.5m; today the figure is over 4m—exactly what it was when he took office four years ago. At nearly 8.3% by the OECD's measure and around 10% by its own calculation, Germany's unemployment rate is one of the highest in the rich world. Now, says Mr Schröder's friend, Peter Hartz, a Volkswagen director who chaired the commission that has unveiled the plan (see page 39), 2m more people will, if his recommendations are acted upon, have jobs within three years.

Phooey—and Messrs Schröder and Hartz should know it. This is not to say that Mr Hartz's suggestions, or at any rate most of them, lack merit. The idea of a "one-stop shop" where the unemployed can both find jobs and get welfare if they fail to do so has worked elsewhere. Giving staff at the newly-named "job centres" incentives for getting their "customers" into jobs is fine. Encouraging more Germans, through tax benefits and with other devices, to take temporary, part-time or low-paid jobs is sensible, as is cutting welfare if people refuse jobs and prefer to stay on the dole (if it is really done). So is pressing the young and single or childless couples to look for jobs beyond their home area. Providing incentives to get people out of the black market and into the legal one is good too.

Nor is it fair to scoff at the chancellor's entire economic record of the past four years. It was not his fault that the global economy slowed to a halt just as he entered his election year, after more than two years of pretty solid German growth and gently falling unemployment. Moreover, he has taken some bold and worthy steps. He embarked on tax-cutting reforms that were radical by Germany's standards. He made a start, albeit tentative but still quite daring for a Social Democrat, towards pushing people into private pension schemes.

It should also be acknowledged that Germany remains the powerhouse of Europe's economy. Its GDP is one-third bigger

than either Britain or France, its closest competitors. German productivity is still high. Most Germans still have an enviably high standard of living. And it is hard to imagine any country in Europe being able overnight, without enormous pain and economic disruption, to embrace some 16m poverty-stricken inhabitants, as happened when East Germany was brought into the fold in 1990. A final point in Mr Schröder's defence is that Germans of nearly all political hues are wedded to the system of consensus and compromise that served them well during the post-war decades of rehabilitation. Their hostility to the idea of moving towards a more liberal economy, with a more free-market cut and thrust, is deep. Had he been bolder, his defenders say, Mr Schröder might well have come unstuck.

Yet he did miss a chance

But there the excuses must stop. Much more radical legislation is needed if Germany is to end its uncustomary stint as the West's economic laggard. The nub of Germany's economic problem goes beyond those aspects of labour-market rigidity identified by Mr Hartz. The country's high wage costs and hugely uncompetitive social-security costs need to be tackled too. Hiring and firing in Germany is still far too difficult. The wage-setting practice whereby whole national sectors set a single rate is a recipe for inflexibility—and has been one reason for eastern Germany's failure to take off after unification. Germany is still mightily overregulated. Nothing illustrates that better than its restricted shopping hours: shopping and business, with a handful of exceptions, are still barred on Sundays. The country, it seems, has not fully woken up to the ways of modern economies.

Mr Schröder's decision this week to put off his much-vaunted tax reforms because of the costs incurred by the recent floods (see page 37) is another worrying signal. It implies that he sees the tax cuts as a dispensable bribe to the middle class rather than an essential tool for economic stimulation. True, the chancellor's opponents do not instinctively promote liberal economics either. But three years ago Mr Schröder made much of his pro-business leanings; as an avowed Social Democratic moderniser, he was well placed, however much his loyalists would have groaned and griped, to force through radical reform. He has failed to do so. This latest bundle of ideas, worthy though many of them are, are indeed too little, and quite a lot too late. ■

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America behind bars

SIR – You say that America “is a society that, statistically at least, is beginning to look a little like early Australia” (“Too many convicts”, August 10th). In fact, it is more like early America. British convicts were transported, mainly into Virginia and Maryland, from 1611 until the revolution and comprised around 10% of the population there. Early Australia (ie, Sydney) was exclusively convict, under the control of a military garrison. It was the arrival of increasing numbers of free settlers that provoked hostility to the programme and ended transportation.

Historically, we know what encourages convicts to rehabilitate: they must be young, non-violent, dispersed into small communities that know what they are up to, compelled to work, remunerated and punished if they abscond or reoffend. It is the patience of the broader community that is tested, just as in colonial America or Australia.

JULIE TOBIAS
Sydney

SIR – Two in five adult prisoners are graduates of institution-based juvenile-justice systems. Rather than rehabilitating our youth, juvenile-correctional facilities train young offenders to be better criminals. Unfortunately, resources are disproportionately channelled toward punitive-corrections policies to the exclusion of effective prevention and intervention programmes.

This under-investment in youth services comes at a high cost; it is estimated that for every youth that drops out of high school for a life of crime and drug abuse, it costs taxpayers between \$1.7m-2.3m, with secure-detention facilities costing around \$200 a day per youth. We now have an ideal opportunity to invest in cost-effective prevention and intervention programmes with proven track records. Model programmes in juvenile-justice reform do exist: the Missouri Division of Youth Services, for example, uses a relatively low-cost, individual-

ised, community-based approach with recidivism rates consistently hovering around 10%, one of the lowest in the country.

MICHELE BYRNES
Centre on Juvenile and Criminal Justice
San Francisco

SIR – I am disappointed that you fail to explore the disconnect between crime rates and the rate of incarceration. You incorrectly say that the imprisonment rate is tied to the crime rate. In reality, America's incarceration rate increased nearly ten fold between 1973 and 2000 at a time when, according to the Census Bureau's National Crime Victimization Survey, the crime rate was relatively flat or falling. As you point out, crime is now increasing, which should be expected during the current economic decline. Your inaccurate assumption that incarceration rates are tied to crime rates greatly underestimates the true horror of what the United States is doing to its underclass by way of imprisonment.

JOEL DYER
Longmont, Colorado

Jenin's massacre myth

SIR – You say that “Palestinians accused Israel of massacring up to 500 civilians” in Jenin (“Naught for your comfort”, August 10th). While this charge is widely attributed to Palestinians—even in Kofi Annan's UN report—we have been wholly unable to locate any direct quote from any Palestinian official making it in any media. The confusion appears to have originated when a Palestinian cabinet minister, Saeb Erekat, told CNN on April 10th of unconfirmed reports that up to 500 people had been killed throughout the West Bank in Israel's “Operation Defensive Shield”.

The next day, the *Jerusalem Post* wrote “Palestinian negotiator Saeb Erekat told CNN that Israel had massacred 500 people in the Jenin camp.” In fact, looking at the CNN transcript

from April 10th, Mr Erekat neither made this claim, nor used the word “massacre”. As a publication that sets a higher standard, we urge you to set the record straight, lest one more myth take root among the countless others that fuel the conflict between Israelis and Palestinians.

ALI ABUNIMAH
NIGEL PARRY
The Electronic Intifada
Chicago

Baseball Mitt

SIR – A picture of Mitt Romney bears the caption “About to catch the prize” (“The talented Mr Romney”, August 10th). An examination of his stance, the placement of his hand and the position of his glove reveals that he is not about to catch anything. Rather, he has just tossed the ball. From its size and arc of flight, I would surmise that Mr Romney is playing slow-pitch softball. Not a good omen. The way to win in Massachusetts is to play hardball.

JOHN WILDE
Greenwood, South Carolina

One China

SIR – You refer to China and Taiwan as two states and accuse China of routinely threatening force against Taiwan (“Full of sound and fury”, August 10th). This is a misunderstanding of the consistent policy of the Chinese government on the Taiwan question, does not conform to historical facts and misleads readers. I deeply regret that, as a well-known worldwide magazine, *The Economist* should commit such mistakes. Therefore, I believe that it is necessary for me to re-elaborate Chinese government policy on the Taiwan question.

Taiwan has been an inseparable part of Chinese territory since ancient times. Most governments in the world, including the British government, recognise that the People's Republic of China is the sole legal government representing China and that

Taiwan is part of China; both the mainland and Taiwan belong to one China. We are opposed to any attempt to split China in any form. Peaceful reunification of the motherland is a set policy of the Chinese government. However, the Chinese government is under no obligation to undertake any commitment to give up the use of force. Our not undertaking to give up the use of force is not directed against our compatriots in Taiwan but against the schemes of foreign forces to interfere with China's reunification and to bring about the “independence of Taiwan”.

It is true that Taiwan is a member of the WTO and the Asia-Pacific Economic Co-operation forum, and that it competes in the Asian and Olympic games, but only with the condition that Taiwan participates as a separate tariff zone, an economy or a sports organisation under the one-China principle but not as an independent state.

GONG JIANZHONG
Press counsellor
Embassy of the People's Republic of China
London

Horse power

SIR – Herman Correa-Diaz (Letters, August 10th) asks “Will [Michael] Schumacher be remembered in 400 years because he drove a racing car and won a sports competition five or more times?” In the second century, Gaius Appuleius Diocles is recorded as having won 1,462 of the 4,257 four-horse chariot races in which he competed. In a mosaic in the imperial baths in Trier, Germany, Polydus and his lead horse, Compressor, are identified as victors. Mr Schumacher needs only to find his Juvenal.

DAVID CROCKETT
Apeldoorn, The Netherlands ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James's Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com

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Middle East and Africa

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attention to detail. You should also show a commitment to working as part of a team. Extensive travel will be required in this role and applicants must be fluent in both English and Arabic. Fluency in French would be advantageous. We offer an attractive compensation package that will fully reflect your skills and experience.

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Susan Venton, Human Resources, Standard & Poor's, Garden House, 18 Finsbury Circus, London EC2M 7NJ or by email: susan_venton@standardandpoors.com or by fax 44 (0) 207 826 3592.

The closing date for applications is Friday, 20th September 2002.

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GOVERNMENT OF THE REPUBLIC OF UGANDA

Ministry of Finance, Planning and Economic Development
Second Economic and Financial Management Project

Positions: Two Audit Experts

The Government of Uganda (GOU) has acquired an IDA credit, which it intends to apply through the Second Economic and Financial Management Project (EFMP II) to improve public expenditure management. The Government intends to carry this out by focussing on improving the efficiency and effectiveness of the public expenditure process.

A significant component of EFMP II will focus on the strengthening of financial management processes and systems that will lead to increased accountability, transparency and better financial management throughout the Government.

The Office of the Auditor General (OAG) has a critical role in the Government's financial management process. The OAG is mandated by the Constitution to audit all the public accounts of Uganda including the ministries, Local Authorities, Parastatals and Government Projects. The Office is required by its mandate to carry out financial and "value for money" audits and report the results to Parliament.

The OAG intends to recruit two (2) professionally qualified auditors to assist in strengthening its oversight capacity in the areas of Financial, Value for Money and Computer Systems Auditing. Each consultant will be expected to have specific expertise in one of the three areas and be able to work in all three areas. They will be expected to assist the specialists in the other disciplines as the need arises.

Each consultant will provide:

- Expertise in international best practice in his or her specific area of expertise
 - Capacity building programmes to ensure the sustainability of these specialist audit activities in the OAG
 - In-house and on-the-job training to OAG staff
- More detailed Terms of Reference for this assignment may be obtained from the Project Coordinator at the address below or visit our website.

Qualifications:

Each of the experts will be a professionally qualified accountant/auditor with current membership in a professional accounting body that is a member of the International Federation of Accountants (IFAC). The experts will be expected to have current knowledge and understanding of developments in International Standards of Auditing (ISA), International Accounting Standards (IAS), International Public Sector Accounting Standards (IPSAS), and an awareness of IMF's Government Financial Statistics (GFS) reporting requirements. They will also be familiar with the requirements of the International Association of Supreme Audit Institutions (INTOSAI).

At least 10 years experience in an audit capacity at a senior management/advisory level is required, a minimum of 5 years of which experience should have been with a government audit office.

The experts will have a working knowledge of Value for Money auditing and IT auditing as well as a solid financial audit background.

An annual renewable contract to a maximum of two (2) years will be offered to the successful candidates. Remuneration is commensurate with terms and conditions for consultants of this level.

The consultants will report to the Auditor General and will be provided with office space and relevant facilities during the assignments.

Deadline for Applications: Friday the 27th September 2002 at 1700hrs

Applications should be sent to: The Project Coordinator, EFMP II, Ministry of Finance, Planning & Economic Development, Finance Building, 2nd floor, Room 24 P.O. Box 8147, Kampala, Uganda.
Telephone: (256-41) 347 804. Facsimile: (256-41) 250 005
Email: efmp@imul.com; rmwanga@afrioonline.co.ug; jetidau@afrioonline.co.ug; Website: www.finance.go.ug



International Cocoa Organization

STATISTICIAN

The International Cocoa Organization (ICCO) seeks candidates for the post of Statistician. ICCO is an inter-governmental organization made up of 19 members from producing countries and 22 members from consuming countries.

REQUIREMENTS

- Candidates shall possess at least an advanced university degree in statistics and economics, including formal training in systems analysis from a recognized university or institution of higher education.
- At least five (5) years post qualification experience in empirical research, preferably connected with primary commodity markets and/or international trade. (Holders of relevant first-level university degrees with substantially longer relevant experience may be considered).
- Knowledge of computers and at least three years experience in programming, systems analysis, multi-user database applications and net-working.
- Familiarity with standard software packages of personal computers and ability to train new users.
- Fluency in English, both written and spoken is a pre-requisite together with a working knowledge of French.
- Excellent interpersonal skills, experience working in a multi-cultural environment and the ability to represent the Organization at senior level.
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Applications shall be submitted in English and include a covering letter, curriculum vitae and recent photograph. The deadline for receipt of applications is **30 September 2002**. Applications are to be addressed to the Officer-in-Charge, International Cocoa Organization, 22 Berners Street, London W1P 3DB, United Kingdom, e-mail: head.admin@icco.org

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Mr Chris Gosling, Director of Human Resources
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Center for Global Security Director

Within the Laboratory's National Security Directorate, the Center of Global Security located in Seattle, WA, USA develops regional partnerships to complement and integrate with the core, environmental, energy, and fundamental science capabilities of the laboratory to address issues of global security. The successful candidate must be a nationally recognized expert in one or more areas of proliferation prevention, homeland security, or regional security. Hands-on experience with the implementation of policies designed to further global security is highly desirable. Must have strong interpersonal and communication skills and a demonstrated ability to work effectively and build partnerships with community, academic, state, and federal leaders as well as with physical and social scientists. Must be able to demonstrate a successful record of building innovative programs and staff capabilities that achieve national recognition. Familiarity with the US Department of Energy, the National Laboratory system, and the Departments of Defense and State is highly desirable. The selected candidate will establish and build the professional visibility and reputation of the Center for Global Security in the areas of global and regional security and homeland security; develop a portfolio of innovative project work that has impact and that is closely coordinated with the science and technology of the Pacific Northwest National Laboratory located in Richland, WA; serve as an effective liaison with the community and region; and build and maintain integration between Seattle-based and Laboratory capabilities. An advanced degree in a technical or political science or related area and 10-15 years of experience and demonstrated success in building and leading multi-million dollar programs that apply science-based capabilities to policy-level national security or environmental issues required. Must possess the ability to be granted and retain a DOE Q security clearance. We offer a competitive salary and benefit package.

For consideration, please submit resume to: <http://jobs.pnl.gov/jobs.asp?req=104344> or frances.podratz@pnl.gov or Frances Podratz, MSIN-K8-15, P.O. Box 999, Richland, WA 99352, USA. PNNL is an EEO/AA employer and values diversity in the workplace. F/M/D/V are encouraged to apply.

United Nations Development Programme



The Government of LAO PDR and UNDP are seeking to recruit the Resident Process Advisor for the SUPPORT TO GOVERNANCE AND PUBLIC ADMINISTRATION REFORM (PHASE II) PROJECT.

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Functions:

The Resident Process Advisor will be responsible for providing continuous advice, support and train the government and selected officials; on the design and implementation of major programs of governance and PAR, on methodologies and practices associated with program and project management, documentation standards, office productivity tools and techniques and, facilitate the national, regional and international transfer of know-how and experiences. (S)he will support in the preparation of work-plans, budgeting, performance assessment, training and workshops, terms of reference and will advise the UNDP on the joint approval and sign-off of the design documents and selection of government candidates as well as of the recruitment of intl. and national consultants. Also will support in the functions of donor coordination and the mobilization of additional funding. (Please refer to our homepage for more information www.undplao.org)

The RPA should have solid experience (15-20 years) in governance and PAR, both regionally and internationally, in program and project management, monitoring and evaluation, in training and workshop facilitation. (S)he should have excellent report writing and communication skills in English and in results oriented, strong team player, adaptability and cultural sensitivity.

Start in October 2002 for a period of one year in Vientiane. Interested candidates should send CVs along with a letter of interest by 30 August 2002 to Human Resources Unit, UNDP, P.O.Box 345, Vientiane, Lao PDR Fax: (856 21) 212 029 or 214 819 Ref: LAO/00/007 - Resident Process Advisor. Only short listed candidates will be notified



U.S.A.I.D./Tanzania

VACANCY ANNOUNCEMENT

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USAID/Tanzania seeks the services of a senior professional with extensive experience in agricultural policy, markets, trade, technology development and transfer, agribusiness, producer support services and food security. The position is based in Dar es Salaam, Tanzania. Candidates should have, at minimum, a Master's Degree in Agricultural Economics or a related field and at least ten years of public and private sector work experience at a senior level designing, managing and evaluating agricultural development/agribusiness activities.

The successful candidate will have strong leadership skills, excellent oral and written communications skills, previous experience living/working in Africa (preferably East Africa) and an appreciation of the value of teamwork. Knowledge of Kiswahili will be an advantage, as will previous related experience in Tanzania.

The appointment duration is two years with the possibility of further extensions. The salary range for the position is US\$70,205-91,265 plus a post differential currently equal to 25% of the base salary. Housing and other benefits are also provided.

Complete details and application materials can be found at: www.usaid.gov/procurement_bus_opp/procurement/psc_solicit/

Applications may be submitted electronically, via fax, or by hard copy delivered to:

The Executive Officer
USAID/Tanzania
50 Mirambo Street
P.O. Box 9130
Dar es Salaam, Tanzania
Phone: 255-22-211-7537
Fax: 255-22-211-6559
E-mail: jfernandes@usaid.gov

Deadline for receipt of applications is 16:00 hours (local time), Monday September 9, 2002.
Late applications may not be considered

UNITED NATIONS



NATIONS UNIES

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The United Nations Secretariat is seeking highly qualified individuals for employment as junior professional officers (P-2 level). For this purpose, a competitive examination will be held in early February 2003 in the following occupational fields:

Economics • Finance • Information Technology • Legal Affairs • Library • Statistics

The competitive examination will be opened for the nationals of the following countries:

Afghanistan	Greece	Niger
Andorra	Guinea	Oman
Angola	Guinea-Bissau	Portugal
Antigua and Barbuda	Iran	Qatar
Australia	Iraq	Republic of Korea
Bahrain	Israel	Samoa
Benin	Italy	Sao Tome and Principe
Botswana	Japan	Seychelles
Brunei Darussalam	Liechtenstein	Solomon Islands
Comoros	Maldives	Tonga
Congo	Marshall Islands	Turkey
Cyprus	Mauritania	Tuvalu
Dem Rep of the Congo	Mauritius	U.S.A.
Djibouti	Mexico	Uzbekistan
Equatorial Guinea	Monaco	Vanuatu
France	Mongolia	Yemen
Gabon	Mozambique	
Germany	Namibia	

In order to qualify for the examination, one must meet all of the following requirements:

1. Be a national of one of the countries listed above.
2. Be no more than 32 years old as of 31 December 2003 (should be born on 1 January 1971 or after).
3. Have at least a first-level university degree relevant to the occupational field mentioned above that one would like to take the examination in.
4. Be fluent in either English or French, the two working languages of the Secretariat. Knowledge of additional official languages of the U.N. (Arabic, Chinese, Russian, Spanish) is an advantage.

All those who believe in the purposes and ideals of the United Nations and who wish to participate in the competitive examination are encouraged to apply.

To receive full consideration, applications should be received by 20 September 2002 by the Examinations and Tests Section at the United Nations in New York (acceptable by e-mail, fax or mail).

Detailed information and application forms may be obtained from the Internet

(www.un.org/Depts/OHRM/examin/exam.htm)

or from below:

United Nations

c/o Receiving Unit, 3-B-20

2003 NCRE, Room S-2575E

Examinations and Tests Section/OHRM

New York, NY 10017, U.S.A.

Fax: (+1) (212) 963-3683

E-mail: OHRM-NCE2003@un.org

Application forms may also be obtained from some UN regional offices.



Half a billion Americans?

WASHINGTON, DC

Demographic forces are pulling America and Europe apart. If the trend goes on, it will fundamentally alter America's position in the world

FORGET transatlantic rifts about trade, Iraq, Kyoto, or the International Criminal Court. These have been thoroughly ventilated. One area of difference has not got the attention it deserves: demography. It may prove the most important of all.

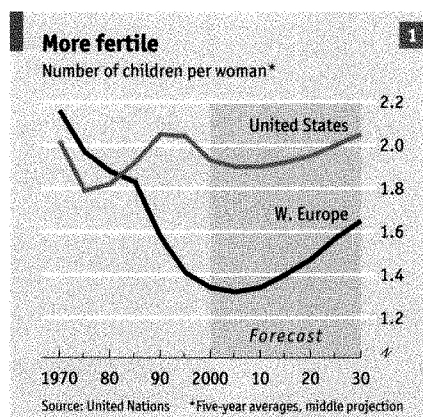
For 50 years, America and the nations of Western Europe have been lumped together as rich countries, sharing the same basic demographic features: stable populations, low and declining fertility, increasing numbers of old people. For much of that period, this was true. But in the 1980s, the two sides began to diverge. The effect was muted at first, because demographic change is slow. But it is also remorseless, and is now beginning to show up.

America's census in 2000 contained a shock. The population turned out to be rising faster than anyone had expected when the 1990 census was taken. There are disputes about exactly why this was (more on that shortly). What is not in doubt is that a gap is beginning to open with Europe. America's fertility rate is rising, Europe's is falling. America's immigration outstrips Europe's and its immigrant population is reproducing faster than native-born Amer-

icans. America's population will soon be getting younger. Europe's is ageing.

Unless things change substantially, these trends will accelerate over coming decades, driving the two sides of the Atlantic farther apart. By 2040, and possibly earlier, America will overtake Europe in population and will come to look remarkably (and, in many ways, worryingly) different from the Old World.

In 1950, Western Europe was exactly



twice as populous as the United States: 304m against 152m. (This article uses the US Census Bureau's definition of "Europe", which includes all countries that were not communist during the cold war. The 15 countries that make up the European Union are a slightly smaller sample: they had a population of 296m in 1950.) Both sides of the Atlantic saw their populations surge during the baby boom, then grow more slowly until the mid-1980s. Even now, Europe's population remains more than 100m larger than America's.

In the 1980s, however, something curious began to happen. American fertility rates—the average number of children a woman can expect to bear in her lifetime—suddenly began to reverse their decline. Between 1960 and 1985, the American fertility rate had fallen faster than Europe's, to 1.8, slightly below European levels and far below the "replacement level" of 2.1 (the rate required to keep the population steady). By the 1990s American fertility had rebounded, rising back to just below the 2.1 mark.

Nobody quite knows why. Some of the recovery was the result of higher-than-average fertility among immigrants. But not all of it: fertility rose among native-born whites and blacks as well. Perhaps the most plausible, if unprovable, explanation is that higher fertility was the product of the economic boom of the 1990s combined with what one might call "social confidence": America was a good country to bring more children into.

America is not unique: a few north-▶▶

▶ European countries, like Norway, have followed a similar trajectory. But it is highly unusual. Nearly every country in the world has seen its fertility rate fall recently and, by and large, the richer the country, the greater the fall. "America", says Hania Zlotnik of the United Nations Population Division, "is the world's great demographic outlier."

Meanwhile, Europe's fertility continues to fall. Having been just below 1.9 in the mid-1980s, the rate is now less than 1.4 and it is projected to continue declining for at least another ten years. In some countries—Spain, Italy and Greece—the fertility rate has fallen to between 1.1 and 1.3.

It is fair to say that these numbers probably exaggerate the long-term demographic difference between the two sides. Remember that between 1970 and 1985 American fertility rates were slightly lower than Europe's. What seems to have happened then was not that Americans were having fewer children overall, but that a generation of women was postponing motherhood. That depressed America's birth rate in 1970-85, shifted a surge of births by half a generation, and produced an unusually high rate in the 1990s. That same population shift is happening in parts of Europe now, especially in those Mediterranean countries with the lowest fertility rates. There too, many women are merely postponing child-bearing. Later, after about 2010, when they have their children, Europe's fertility rate will nudge back up (see chart 1 on previous page).

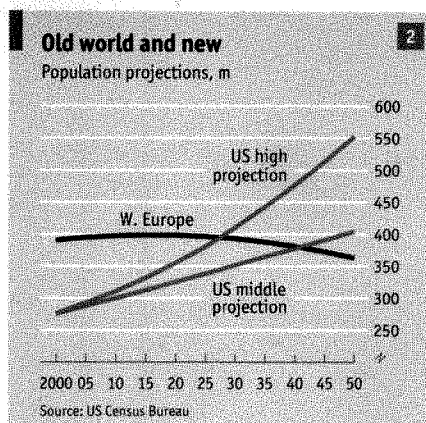
But what is striking about the American rate is not that it rose and fell, but that it rose so much—to within a whisker of the replacement level. And what is striking about the European rate is that it fell so far, to a much lower level than America's. That is also a reason for thinking it may not recover as strongly as America's did.

The UN reckons that the differences in fertility between America and Europe will continue over the next few decades. America's high rate is expected to remain relatively stable. Europe's should recover a bit—but it will not close the gap. The result of these differences, already evident in the census of 2000, will then become starker.

Absolute numbers

America's population should have been 275m in 2000. At least, that is what the central projection of the 1990 census predicted. The 2000 census showed it was actually 281m, higher even than the "high series" projection from 1990. Some of this may have been caused by things other than population change: improvements in counting, for instance. But not all. The new census showed that immigration was higher than expected, and that the birth rate of native-born Americans was up too.

Those higher fertility rates will have a bigger impact as time goes on. By 2040, us-



ing the new census's "middle series" projection, America's population will overtake Europe's. This forecast has already proved too low. On the "high-series projection", the crossing point occurs before 2030 (see chart 2). Admittedly, this projection is based on high assumptions about fertility rates—over 2.5 in 2025-50. But if this proves correct, Europe's population in 2050 would be 360m and falling, America's would be over 550m and rising. Half a billion people: in other words, America would be twice the size it is now. Europe would be smaller. Obviously, straight-line projections over 50 years need to be taken with plenty of salt. All the same, the numbers are startling.

European commissioners are fond of boasting that the European Union (EU) is the largest market in the world. They claim an equal status with the United States in trade negotiations as a result. Some also think that, because of this parity, the euro will one day become an international reserve currency to rival the dollar.

But assume, for a minute, that Americans remain, as they are now, about one-third richer per head than Europeans. The high-series projection implies that America's economy in 2050 would still be more than twice the size of Europe's—and something like that preponderance would still be there even if you assume that by then much of Central and Eastern Europe will have joined the EU. The balance of global

economic power would be tilted in fundamental ways. With 400m-550m rich consumers, the American market would surely be even more important to foreign companies than it is today. And if so, American business practices—however they emerge from the current malaise—could become yet more dominant.

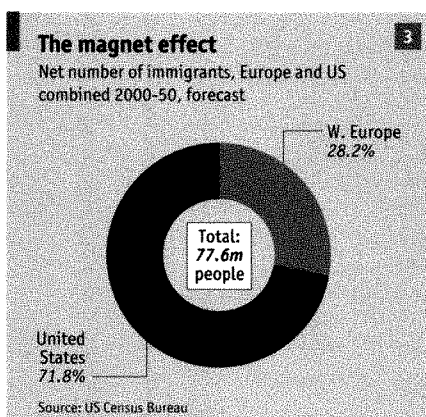
And still they come

Part of the rise in the population has been driven by higher fertility. The rest comes from immigration. In the past decade, America has taken in over 11m immigrants. That compares with 6m in the 1970s and 7m in the 1980s. The real number of new immigrants may be even higher, since these figures may not account for all the estimated 8m-9m people who have slipped illegally into the country. Some may return home. Others may be thrown out. But those that remain contribute to the growing population both directly and indirectly (that is, through their children). The fertility rate for non-hispanic whites is just over 1.8, for blacks 2.1. For Latinos, it is nearly 3.0—higher than in many developing countries. From the point of view of the overall population, therefore, higher immigration counts twice over.

That is a reason why America's total population will continue to rise, though perhaps not as much as the highest estimates suggest. Many of the new migrants come from Mexico. If Mexico's own demographic pattern, with fast-falling fertility, is anything to go by, the fertility rate for American Latinos is also bound to fall, though it will still be quite high.

Europe has had an immigration boom as well, of course. Indeed, in 1985-95, there were slightly more immigrants going into Europe than into America (though since Europe's population is larger, America's rate was higher). But more recently, the European numbers have fallen—presumably reflecting increased barriers to entry—and overall, since 1950, Europe has taken in far fewer people. Most demographers forecast that immigration will be much lower in Europe than in America during the next few decades (see chart 3).

The difference in immigration not only increases America's population compared with Europe's, it also makes it look increasingly different. Compare the different shapes of chart 4 (on next page), which maps the age distribution of America's whites, on the left, and other groups, on the right. Whites form a pear shape: they are preponderant among adults. This is also the shape of Europe's population. Blacks and browns form a pyramid: children account for most of the population. Even now, in the parts of America with the highest immigration, such as Los Angeles and Houston, Latinos account for half of all children under 14. This is the charac- ▶▶



► teristic shape of developing countries. As the bulge of Latinos enters peak child-bearing age in a decade or two, the Latino share of America's population will soar.

That could have an impact both on economics and on geopolitics. The economic impact is clear enough. Kenneth Prewitt, the former head of the US Census Bureau, argues that "in the struggle to find workers to support growing economies, nations that are hospitable to immigrants will have an advantage." Immigrants go where there are friends and family to welcome them and help them get jobs. Where will they find a more hospitable welcome—Europe or America?

The geopolitical impact is fuzzier, but still powerful. At the moment, America's political connections and shared values with Europe are still strong, albeit fraying. But over time, America's ties of family and culture will multiply and strengthen with the main sources of its immigration—Latin America chiefly, but also East and South Asia. As this happens, it is probable that it will also pull American attention further away from Europe.

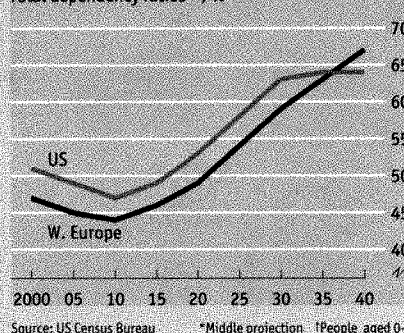
The young world and the old

Higher fertility rates and immigration produce not only a larger population but a society that is younger, more mixed ethnically and, on balance, more dynamic. The simplest expression of this is median age (by definition, half of the population is older than the median age, and half younger). According to Bill Frey, a demographer at the University of Michigan, the median age in America in 2050 will be 36.2. In Europe it will be 52.7. That is a stunning difference, accounted for almost entirely by the dramatic ageing of the European population. At the moment, the median age is 35.5 in America and 37.7 in Europe. In other words, the difference in the median age is likely to rise from two to 17 years by 2050.

Behind this change lie demographic patterns with big policy implications. The percentage of children in the population is falling as populations age. But in America it is falling more slowly than elsewhere. In

Grannies or guns?

Total dependency ratios*1, %



Source: US Census Bureau

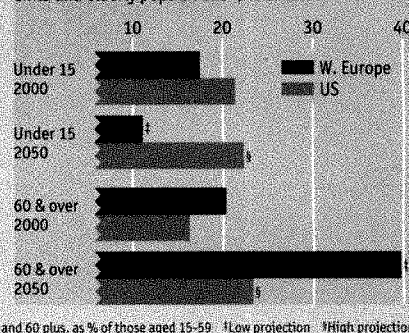
*Middle projection

†People aged 0-14 and 60 plus, as % of those aged 15-59

‡Low projection

§High projection

Child and elderly populations*, % of total



1985, America and Europe had more or less the same proportion of the population under 14 years of age: around 20%. By 2020, the proportion of children in Europe will have slumped to 13.7%. In America it will still be 18.6%—not only higher than in Europe but higher than in China and Japan, as well.

From a fiscal point of view, more children are not necessarily a blessing: their education is a burden on the public finances. Because America has relatively more children than Europe, its "dependency ratio", or the number of children and elderly people for each working-age person, does not stay low. It is slightly higher than in Europe now—51% against 47%—and will stay just above European levels as the ratio rises in both places until about 2035 (see left-hand panel of chart 5). But note the difference: a higher proportion of Europe's "dependency costs" comes from the old. The number of people over 65 will be equivalent to 60% of the working-age population in Europe in 2050, compared with only 40% in America. There, most of the overall burden will come from the cost of educating children (chart 5, right-hand panel).

You see the significance after 2035. In America, the dependency ratio will start to fall as the bulge of children turns into a bulge of adults. But in Europe there will be no such change, and the ratio will continue

to rise. This is where the implications for public policy become large.

Both Europe and America face fiscal problems in providing pensions and health care as their baby-boomers retire. On some estimates, by 2050, government debt could be equivalent to almost 100% of national income in America, 150% in the EU as a whole, and over 250% in Germany and France. So while the burden is growing on both sides of the Atlantic, it is much heavier in Europe.

That is a problem in its own right, and a source of another long-term difficulty in the transatlantic relationship. Since the end of the cold war, Europe and America have made different calculations about where to spend public money. America has put more into defence; Europe has spent more on social programmes.

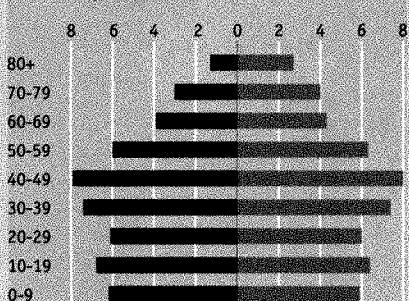
The result is a familiar military imbalance. America spends about twice as much on defence as the entire European Union (\$295 billion in 2000, or 3% of GDP, compared with the EU's \$153 billion), thus maintaining its preponderant military might. Europeans intermittently promise to spend more in order to narrow the military gap, recognising the dangers to the NATO alliance if they fail to pull their weight, but population trends will sap their determination.

If Europeans are unwilling to spend what is needed to be full military partners of America now, when 65-year-olds amount to 30% of the working-age population, they will be even less likely to do more in 2050, when the proportion of old people will have doubled. In short, the long-term logic of demography seems likely to entrench America's power and to widen existing transatlantic rifts.

Perhaps none of this is altogether surprising. The contrast between youthful, exuberant, multi-coloured America and ageing, decrepit, inward-looking Europe goes back almost to the foundation of the United States. But demography is making this picture even more true, with long-term consequences for America's economic and military might and quite possibly for the focus of its foreign policy. ■

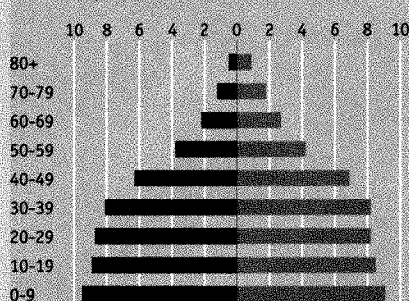
Browner means younger

Age distribution of the white* population
United States, 2000, %

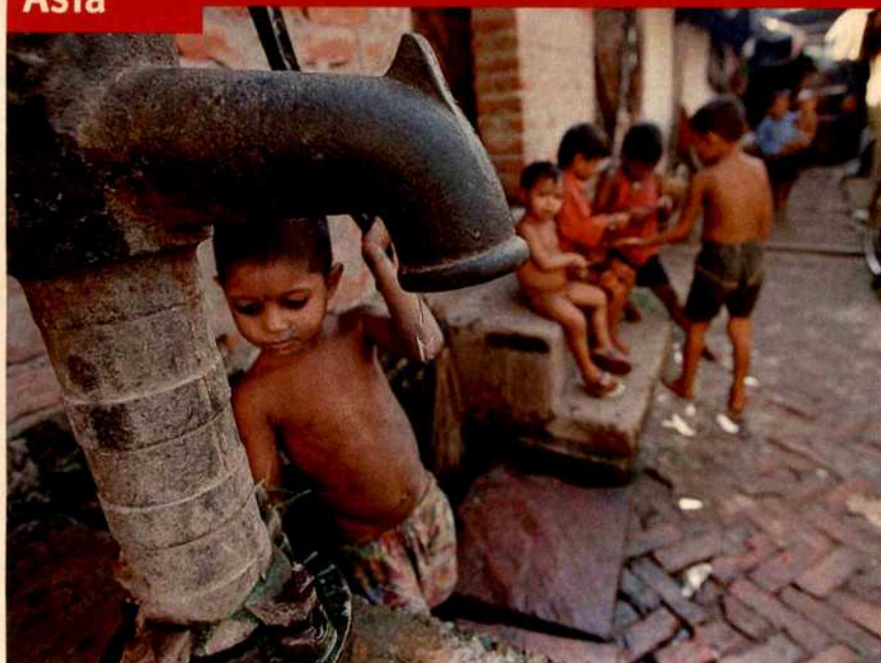


Source: US Census Bureau

Age distribution of the non-white population
United States, 2000, %



*Excluding Latinos



Water in India

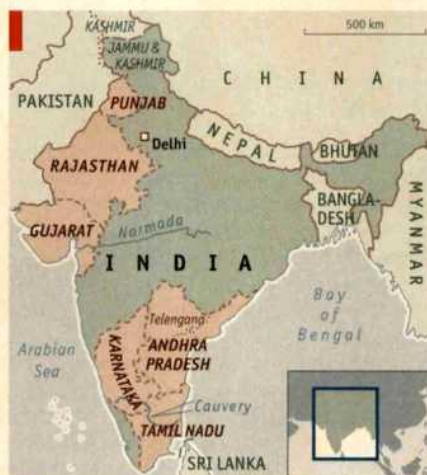
Nor any drop to drink

DELHI AND HYDERABAD

India has plenty of water, but lacks good systems—political as well as infrastructural—for allocating it. Andhra Pradesh is pointing the way

CHILI is expensive to grow. So last year, when Boda Balu's 1½ acres were not getting enough water, he went up his canal with an axe to where a richer farmer was drawing off water and smashed his pump. Y. Ranga Reddy, president of a water distribution committee on a nearby canal, is alarmed about pump-smashing on a grander scale. The government of Andhra Pradesh, the southern state where both he and Mr Balu live, is releasing dam water for electricity generation, rather than supplying it to the farmers of the water-starved Telengana region. For the second year running a scant monsoon threatens their crops. "If the situation continues there might be a point where people will destroy the electricity company," he says.

All of India, not just Andhra Pradesh, is prone to water rage. Louder versions of Mr Balu's spat are occurring within states, between states and between different sorts of water consumer. They are bound to get worse. India is expected to have another 400m people by 2025; industry and households will demand a larger share of fresh water from agriculture, which now consumes 85% of it. Nearly three-quarters of Indians will then be living in regions with less than 1,000 cubic metres of water (264,000 American gallons) per person per year, too little to sustain economic development. The government is aware of this slow-motion crisis, but unprepared.



India as a whole is not parched. It has substantially more water per head than Korea and South Africa. It grows enough food to feed itself even when the monsoon disappoints. The trouble is that India gets most of its water during the four-month monsoon, that some areas have far less than others and that it is mismanaged. The World Bank points out that drier countries than India have higher agricultural yields and more water available for drinking, sanitation and industry.

India's policies practically guarantee mismanagement. In Punjab, India's breadbasket, price supports and free electricity

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24 A war crime in Afghanistan?

encourage farmers to grow water-guzzling rice, oblivious of the threat to the soil's fertility. Half of India's villages have inadequate drinking water.

Water is virtually free to most consumers, but their rights are fuzzy. Groundwater belongs to the owner of the land on top of it; surface water is the property of the state, which is loth to charge consumers anything close to the price of supplying it. Bureaucracies are too poor and indifferent to administer it efficiently or fairly. India's canals lose 70% of the water they carry before it gets to the consumer. Under the constitution, water is mainly the business of the states, not the central government. Their quarrels are bitter. The southern state of Tamil Nadu claims that neighbouring Karnataka violates commitments to share water from the Cauvery river. "If the Cauvery problem is not solved," wrote one Tamil Nadu MP this month, "Tamil Nadu could go the way of Kashmir."

Arguments about what to do are equally acerbic. Some non-governmental organisations see the answer in mobilising local communities to harvest rain and develop watersheds. Thus, even the wastes of Rajasthan can bloom. Such initiatives can extend water rights to people who have traditionally lacked them, such as landless labourers. Activists are usually hostile to the government's traditional reliance on big projects, especially dams like the one planned across the Narmada river. "Privatisation" is also anathema: water is a social good, not an economic one.

There is a sensible synthesis, which is what the central government largely supports. This treats water as both an economic and a social good, favouring prices that encourage investment and conservation as well as subsidies to protect the poor. It advocates giving a role in the allo-

K.P. -1326

Floods in Asia

China's lake of menace

BEIJING

And high tides threaten Bangladesh

WHEN it's not a drought, it's a flood. In China this year, more than 900 people have died in floods, and officials fear that the toll could eventually exceed that of the 4,000 deaths in 1998. Emergency services in south China's Hunan province went on high alert this week on worries that rain-swollen Dongting Lake, 2,700 square kilometres (about 1,000 square miles), the size of Luxembourg, would burst its banks and threaten the lives, homes and farmland of 10m people. The lake's water level is the highest for three years. As in 1998, thousands of soldiers are standing by.

Flooding plagues much of southern China in the summer storm season, particularly along the Yangtze River and its tributaries. But while the south gets too much water, the northern and western provinces suffer from drought. In July,

the government approved a colossal scheme aimed at evening things out. China plans to spend more than \$50 billion to dig three canals, each one 600km (375 miles) long, that between them will carry 48 billion tonnes of water annually from the Yangtze to the north.

The project is controversial. It will displace an estimated 250,000 people, and some experts fret that tampering on such a massive scale with the nation's river systems could bring unforeseen consequences. But given the alarming news from south China this week, the temptation is indeed understandable.

Meanwhile, Bangladesh, to China's south, is suffering from the habitual flooding that accompanies the monsoon. This week exceptionally high tides made at least 50,000 people homeless along the Bay of Bengal.

has no clear plan for ending a decade-long economic slump, and has steered its youthful prime minister, Junichiro Koizumi, away from every popular idea he ever endorsed.

For the Democrats, the tantalising fruit of real power is dangling about as closely within reach as it can get. Yet the party still seems to lack the stature to reach up and pluck it. Despite everything, it trails the LDP by 23 percentage points in opinion polls. And its two main leaders, Yukio Hatoyama (its distinctly lacklustre current president and party leader) and Naoto Kan (the secretary-general, and the most popular Democrat among the general public) have no convincing strategy for winning over unaligned voters.

That pitiful opposition showing is the driving force behind the younger MPs' gamble—actually, two gambles. First, the four youngsters, three of whom are in their early 40s, may be risking bright futures by sticking their necks out this time around, rather than simply biding their time. The leadership race will already feature several senior members of the party, including Mr Kan (with 26% national support) and Mr Hatoyama (17%). The four young Democratic hopefuls, by contrast, pull 1-2% support each among the wider public.

The other gamble is less a personal risk than a party one. If any of the young contenders does manage to seize the top post, say the stalwarts, they risk splitting the very party that they hope to ride into office. Formed during the tumultuous realignments of the mid-1990s, the Democrats comprise former factions of several other parties, from the LDP itself to the Socialists. Its rough platform tries to bind these factions together by combining a call for greater competition with plans to extend the safety net under those who lose their balance in the upheaval. When Mr Kan labelled this amalgamation “the party of Thatcher and Blair”, he appears to have meant it as a good thing.

Most disgruntled young Democrats favour more emphasis on the competition side of the economic-reform ledger. Their current leaders, they complain, are too ▶▶

▶ cation of water to organisations that span river basins, which normally cross state lines. And it champions participation by water users, especially farmers. Here, Andhra Pradesh is India's role model. In 1997 it began a revolutionary restructuring of irrigation, handing over control of canals to 10,000 “water users' associations” (WUAs), groups of farmers who elect leaders to manage the system.

Is it working? Clearly, some good has been done. The World Bank paid for a burst of repairs that unclogged and strengthened canals, allowing water to reach fields that had been cut off for years. Andhra Pradesh's energetic chief minister, Chandrababu Naidu, boldly tripled water charges. Although they are still below the cost of supply, they do provide WUAs with funds to maintain the canals.

It is less clear that the associations have democratised control of irrigation. Their presidents, though elected, are usually the same people who have always run the show. One study of five WUAs found that 85% of their executives had landholdings of more than four hectares (ten acres), much larger than average. Many presidents are contractors for canal works; corruption, or at least the suspicion of it, is rife. The government claims that irrigated areas expanded by 700,000 acres in the first two years of the reform. “We can't find it,” says Peter Mollinga, a Dutch academic. What gains there have been, he thinks, come from the World Bank-financed repairs, not any increase in clout for weaker farmers. That, after all, is why Mr Balu took an axe to his neighbour's pump. ■

Japan

Enter, at last, a gang of four

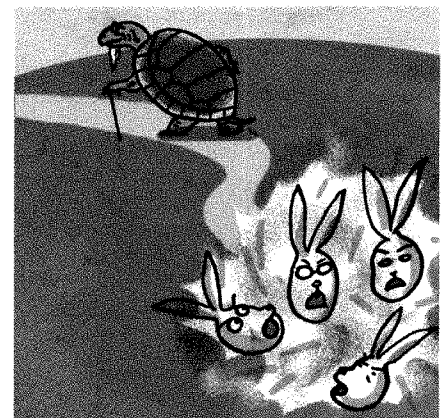
TOKYO

Young reformers hope to whip the opposition into shape

JAPAN'S predicament, as everyone knows, is dismal. A decade of flat or negative growth, record unemployment, a collapse in asset prices: in most countries, these would surely spell political death for the party that had presided over the mess. Yet the leaders of Japan's Democratic Party, the biggest in the opposition, seem poorly equipped to take advantage of what ought to be a highly favourable political setting. Young Democrats such as Shigefumi Matsuzawa, 44, the eupneptic representative for Kanagawa, believe it is time to change that.

At the next election for party president, on September 23rd, Mr Matsuzawa hopes to turn Japanese politics on its head by replacing the Democrats' familiar leaders with one of the four little-known young members—preferably himself—who have recently tossed their hats into the ring. “We are in a time”, he says plainly, “when we have to gamble.”

In a healthier democracy, knocking off a ruling party as corrupt and enfeebled as the Liberal Democratic Party would hardly require much of an appetite for risk. The LDP has been battered by a storm of recent scandals. Many of its top people are old. It



quick to compromise with labour unions, parts of the bureaucracy and other interest groups that are opposed to bankers and executives but do not necessarily favour freer markets. Because these groups are also content with Japan's corporatist economy, the youngsters argue, the Democrats cannot tear into the LDP's policies as viciously as they should.

If they are going to take on these leaders, however, the youngsters must first whittle down their list of challengers. After meeting again on August 20th, a group of 50 young Democrats still could not get any of the four to drop out. The two front-runners, Seiji Maehara and Yoshihiko Noda, have locked up the 20 MPs they need to back a leadership bid; but Mr Matsuzawa and Takashi Kawamura (a maverick businessman, and at 53 the oldest of the group) have yet to bow out. A simple vote among young Democrats seems too hard to agree upon.

Their slowness in whittling down the field to a viable one candidate suggests that, in one crucial sense, the junior Democrats may not be too different from the leaders they aim to supplant. When talking about the current stalemate, they exude less a real sense of urgency than, at best, a theoretical appreciation of the merits of acting urgently. But if they cannot speedily sort out their leadership bid, the young Democrats will surely fall together, and their party will have missed a golden opportunity to renew itself. The same might be said, perhaps, for Japan. ■

Indonesian justice

Just doing their duty?

JAKARTA

Verdict on the East Timor trials

IF THERE is one subject on which foreigners and Indonesians misunderstand one another, it is East Timor. In 1999, foreign diplomats hoped they had sealed an agreement with the Indonesian government when it agreed to hold a referendum on the province's future. But when the East Timorese opted for independence, local militias, helped by Indonesian soldiers and bureaucrats, put the place to the torch.

Foreign governments were outraged. They thought they had secured some restitution in 2000 when Indonesia agreed to try those responsible for the violence. But the tribunal set up for the purpose has now handed down its first verdicts, and it looks as if the world is in for another nasty surprise. On August 15th, a policeman and four soldiers accused of complicity in a massacre, and Timbul Silaen, East Timor's



Just chums, really

police chief at the time of the referendum, were all acquitted. The day before, Abilio Soares, the province's governor in 1999, had been sentenced to three years, thought by critics to be unduly lenient. Many of the remaining 16 defendants are expected to go free.

The government has taken a half-hearted approach to the tribunal. The law creating it limited its scope to the events of a few months and a few districts of East Timor. The attorney-general's office decided not to prosecute almost half those put forward by Indonesia's National Commission for Human Rights. The government appointed inexperienced judges to hear the cases. Prosecutors called few hostile witnesses. In the case of Timbul Silaen, they summoned only two Timorese to the stand, both of whom testified that the accused was not such a bad egg. Above all, the prosecution did not really challenge the defence's contention that the authorities were bystanders, rather than orchestrators of the conflict.

Human-rights activists, citing the verdicts as proof of the Indonesian tribunal's inadequacy, are now calling for some sort of international body to be set up, akin to those trying war-crimes suspects from Rwanda and Yugoslavia. But that seems unlikely, since many of the countries that pushed for the trials in the first place now have other concerns. America is keen to keep Indonesia's backing for the war on terror. Donald Rumsfeld, its secretary of defence, praised the tribunal during a visit to Indonesia in February. Even the Timorese themselves seem ready to let bygones be bygones, in the interest of national reconciliation and good relations with their giant neighbour. Xanana Gusmao, the new country's president, sent the tribunal a letter appealing for clemency in the case of Mr Soares.

Such discretion may be a wise course for East Timor, but may not make Indonesia a better place. Senior army officers visited the tribunal to show their support for the accused, who, according to the armed-forces' commander, had only been doing their duty. Indonesian soldiers continue to commit abuses in restive provinces such as Aceh. Meanwhile, many Indonesians believe that their country was and is the victim of an international conspiracy to dismember it. That sets the stage for more misunderstandings to come. ■

Pakistan

Five more years

LAHORE

The dictator awards himself a new term

IF YOU want to keep the army out, you have to bring it in." Thus, surreally, spake General Pervez Musharraf, Pakistan's latest Bonaparte, at the televised press conference on August 21st at which he announced his own coronation as president, army chief and chairman of a powerful new National Security Council for the next five years.

In the same breath, he insisted that neither he nor the army would have anything to do with actually running the country. As president, however, he will have the power to sack parliament, and the provincial governors appointed by him will have the power to sack provincial parliaments. The NSC will comprise the three service chiefs and the chairman of the joint chiefs of staff, as well as the prime minister, the leader of the opposition, the four chief

► ministers and the chairpersons of both houses of parliament. The general will chair—and dominate—this powerful body.

The constitutional amendments have been carried out under the cover of a "legal framework order" issued on August 21st that simply inserts a new article (270A) in the constitution to validate all acts by his government since it seized power at gunpoint in October 1999.

"The supreme court has permitted me to do so. If anyone wants to challenge this, he can go to the supreme court," the general said, in ruling out a demand by the political parties that his amendments should be validated by the next elected parliament. "I don't need parliament's approval for these amendment." However, he said that parliament will have the power to undo them by a two-thirds majority.

But there is a catch. For he also says that if the next parliament tried to gang up against him and the NSC, he would be forced to choose between resigning or sacking the parliament. No prizes for guessing which it would be. With the opposition having denounced the move as illegal, writs are bound to fly thick and fast.

Still, at his press conference, General Musharraf told citizens to look on the bright side. He claimed that more than two-thirds of the constitutional amendments proposed by his government a month ago had been dropped in response to public feedback. These included a measure that would have enabled him to appoint and remove prime ministers (though since he can dissolve parliament, this concession may be moot.) "This is a critical transition period from democratic dictatorship to an elected democracy," he averred.

Powerful he may be: but not safe. Fears of assassination are confining the general to the capital, Islamabad. A speaking engagement in Karachi this month was cancelled at the last minute on the advice of intelligence chiefs. General Musharraf has become a prime target for al-Qaeda terrorists and their Pakistani allies since the government began helping American agents track them down. In April, officials say, a group allied to al-Qaeda planted a car bomb on a road taken by General Musharraf in Karachi. It failed to explode.

Pakistan has become a dangerous place for anyone with western links. In January, an American journalist, Daniel Pearl, was kidnapped and murdered. In March five people, among them two Americans, died in a grenade attack on a Christian church in Islamabad. In May, a bomb in Karachi killed 14 people, 11 of them French technicians. Pakistan's intelligence agencies now fear that government officials may be the next targets of al-Qaeda in a move to destabilise the country in the run-up to the general election in October. Uneasy lies the head that wears the (stolen) crown. ■

A war crime in Afghanistan

Dead on arrival

Did America's Afghan allies deliberately suffocate prisoners?

TO FIGHT the Taliban, America has relied on local allies who may be war criminals. *Newsweek* claimed this week that almost 1,000 fighters who surrendered to Northern Alliance forces in November were crammed into sealed containers and deliberately condemned to a slow death while being transferred to the Sheberghan prison near Mazar-i-Sharif. Their bodies, according to the report, were then dumped in a mass grave near the prison. There is now mounting pressure on local and international authorities to uncover the truth.

The presence of what appears to be a mass grave at Dasht-e Leili, near the prison, has been known for a while. Physicians for Human Rights (PHR), an advocacy group which took a look at mass graves near Mazar-i-Sharif in January, concluded that this one contained recent human remains, and locals have told the group that a large number of Taliban prisoners were buried there. In April the UN sent a forensic team to the site. The examination revealed that the victims died by suffocation. For the past six months, PHR has been calling for a full investigation, without any success, so the allegations have still not been verified.

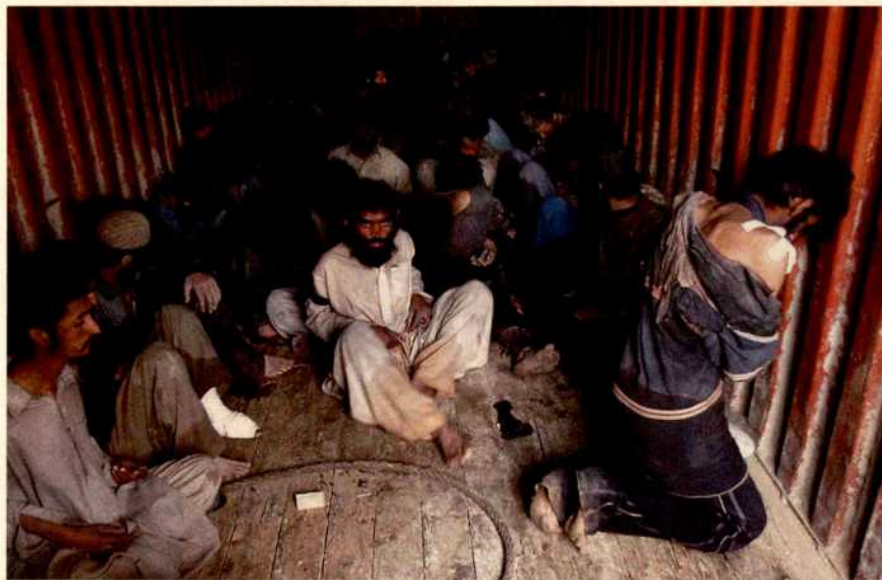
America's defence department says that although there were American forces in the area at the time, no one has any knowledge of the alleged crime. PHR was told earlier this month by Joseph Collins, a

deputy assistant secretary of defence, that the Pentagon would take no action to secure the site or investigate it.

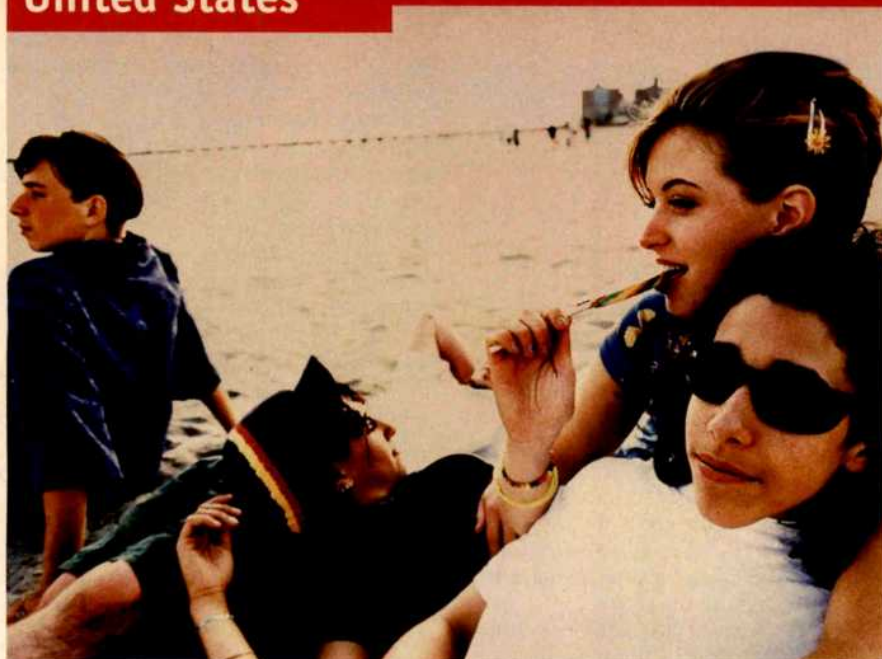
Even for those who made it to Sheberghan alive, life has not been pleasant. Under the authority of Abdul Rashid Dostum, a notorious local warlord and former deputy minister of defence, the prison is a byword for the mistreatment of prisoners. Following the defeat of the Taliban in the north, the prison—with an estimated capacity of less than 1,000—held about 3,500 men. In January, PHR reported severe overcrowding, appalling sanitary conditions, dysentery and malnutrition.

The situation appears to have improved a bit since then, thanks to the intervention of the Red Cross. The release of over 2000 of prisoners has reduced the overcrowding. The fate of those still behind bars, however, is unclear, as the Afghan judiciary is in no position to deal with them. What will happen to the 75-odd being held by coalition forces in Kandahar and Bagram, in addition to the 550 who were transferred to Guantanamo Bay, is no less uncertain. None of them has been charged with any crime.

Pending a full investigation, it is difficult to be sure what happened at Dasht-e Leili, or at the many other mass graves around the country. And investigating is no minor endeavour. Security is dicey. No credible protection can be offered to witnesses. Neither the Afghan government nor the outside world has decided on how to deal with alleged war criminals. Leonard Rubenstein, executive director at PHR, insists that the potential enormity of this crime warrants some action. Sooner or later, its perpetrators should have to answer for their actions. The question the Americans might have to answer is whether they should have kept their Afghan allies on a much tighter leash. ■



Another containment strategy



The jobs market

The young and the rested

DEERWOOD, MINNESOTA

One part of the American workforce is hurting badly—teenagers

THROUGHOUT its 104-year history, Ruttger's Bay Lake Lodge has employed a lot of teenagers. Each summer, around two-thirds of the 325 staff at the remote holiday resort are high-school and college students. The end of August sparks a crisis: the students go back to school, leaving Ruttger's, which closes in November, scrambling to find dishwashers, waiters and housekeepers.

This year, the resort's managers are less frantic than usual. Before Ruttger's opened in April, it got an uncharacteristically high number of applications from adults, even though many of its jobs pay below \$7 an hour. Ruttger's is thus employing around 25% fewer teenagers than normal, even though they also applied in droves.

American teenagers are an atypically industrious lot. In most developed countries, teenagers work only if the family needs income. Yet the American teens most likely to work have historically been white, attended college, lived outside a big city, and (perhaps most surprisingly of all) had a family income above \$40,000 a year. By contrast, poor inner-city kids have been much less likely to hold jobs.

A new report by the Centre for Labour Market Studies at Northeastern University in Boston points out that this has been the toughest summer-job market for teenagers in 37 years (see chart). The problem extends beyond seasonal work. Many starter

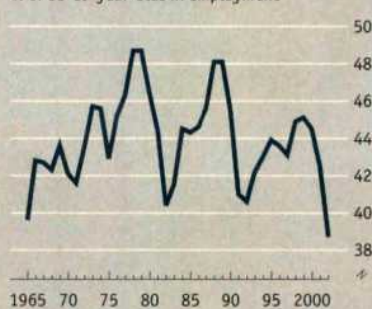
jobs once filled by America's youth—at cash registers, griddles, dishwashing stations and on newspaper routes—have now been nabbed by adults.

The unemployment rate for people aged 16-19 (and seeking work) was 17.7% in July. That compares with 14.8% in the same month last year and 13.4% in 2000. More tellingly, if you include those who have given up looking for work, the employment-to-population (EP) ratio for teenagers has dropped to 38.7% this summer, compared with 44.5% two years ago. Andrew Sum, a professor at Northeastern, sees a "depression" in the teen-labour market.

Such language is a little dramatic. The employment situation varies by state, and

Summer days, drifting away

% of 16-19-year-olds in employment*



Source: Bureau of Labour Statistics *For July in each year

Also in this section

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even within states. Richard Judy, an economist, points out that in regions such as central Illinois and the Tampa Bay area in Florida, there are too few people to fill unskilled jobs. Others think that teenagers are simply concentrating on different things: a new report by the Bureau of Labour Statistics says more teens are studying during the summer than in past years.

That might perhaps help to explain the changing EP ratio for teenagers, but it does not explain rising unemployment among those teens who want to work. A lot of teens looking for jobs are not finding them. How much is this due to the current economic downturn and how much to deeper structural changes in the workforce?

The experience of teenagers hints at something of a crunch in service jobs at the bottom of the employment ladder. Some labour-market experts argue that lay-offs, or fear of them, have persuaded adults to take jobs which were once filled by college graduates, pushing some of the latter back down into jobs once held by high-school graduates and dropouts.

Minnesota, for instance, actually has one of the country's highest rates of teen employment (alongside Iowa, Nebraska, and Wisconsin). But job vacancies in Minnesota in the second quarter of this year were 41% below the same period last year. That prompted many adults to look for jobs once held by less skilled workers.

Another factor has been Wall Street. The drop in personal savings caused by the stockmarket plunge has prompted many older Americans either to postpone retirement or re-enter the job market. According to the AARP (formerly known as the American Association of Retired Persons), there are 8% more Americans above the age of 55 working now than there were a year ago. Many are in skilled fields such as consult- ▶▶

ing; but plenty are also doing odd jobs part-time. However, there are also longer-term forces at work:

- **Immigration.** The surge of new immigrants over the past decade has created a huge new labour pool, mainly along the east and west coasts and in big cities like Chicago. Many have little education: about a third lack a high-school diploma, three times the rate of native-born Americans. Many speak little English, and thus qualify only for the unskilled, low-wage jobs that teens used to pick up.

- **Welfare reform.** In 1996, Congress passed a law requiring welfare recipients to work or get job training in exchange for benefits. The number of people on welfare has dropped from 14m in 1994 to 5m today. Many who went from welfare to work were unskilled and took entry-level jobs.

- **Demography.** There is an unusually large number of teenagers around, thanks to a "baby-boom echo"—a generation born to the original boomers between 1977 and 1994. Tom Dilworth, a labour expert with the Employment Policies Institute in Washington, DC, points out that around 35m echoers had turned 16 by last year ("eligible worker" age). They now account for around a fifth of the total workforce. The EPI estimates that by 2010, nearly 74m members of the echo generation will be 16 or over, accounting for about 37% of eligible workers. An ever-increasing number of these young workers are Latinos.

Smells like teen spirit

A teenager having trouble finding a job might seem a harmless form of preparation for the rigours of the "proper" job market; after all, few are their family's primary wage earners. But there is now quite a lot of research arguing that such experiences can have serious consequences. A 2001 study for the EPI by Thomas Mroz and Timothy Savage from the University of North Carolina at Chapel Hill linked teen joblessness to lower lifetime earnings, future unemployment and a variety of other social ills.

Inevitably, there have been calls for special help. Northeastern's Mr Sum, for instance, wants a federal jobs-stimulus programme for young Americans. Others argue that some proposed laws are actually damaging chances for teens. Mr Dilworth at the EPI points to a health-insurance bill proposed by Senator Edward Kennedy, which he says would make it more difficult for employers to hire teens.

Naturally, some things may improve if the economy does. But some things have probably already changed forever. These days, Mr Judy notes, "paper delivery by kids on bikes is something out of Norman Rockwell". But perhaps it was inevitable that adults would take over the newspaper routes. How many teens want to get up at 5am anyway? ■

Coffee politics

Lovin' cups

BERKELEY, CALIFORNIA

Coffee, and justice, for all

BERKELEY is the birthplace of People's Park and of American coffee snobbery. So it seems fitting that the city's peace-loving, caffeine-wired citizens are embracing a way to combine their politics with their drug of choice (or one of them, anyway). "Sec C"—short for Socially and/or Environmentally Consciously Cultivated Coffee (and pronounced "sexy", of course)—is a proposal to limit the kinds of coffee sold in Berkeley, and is up for discussion on the November ballot.

America's speciality-coffee revolution kicked off in the late 1960s in Berkeley, where Alfred Peet, a Dutch immigrant and founder of Peet's Coffee, trained the men who would later start Starbucks in Seattle. Nowadays cafés line most of Berkeley's main streets, and people discuss coffee blends with the passion of wine-tasters. Yet no one can agree on Sec C.

The initiative is the hobby-horse of Rick Young, a lawyer fresh from the University of California at Berkeley's law school. After successfully persuading the owner of the law-school café to switch to more politically-correct coffee, Mr Young decided to take the matter to the streets. Having collected over 3,000 signatures, he is now in a position to appeal to the university town's 80,000-odd voters.

If passed, only coffee beans that are certified as organic, fair-trade or shade-grown could be sold. To brew regular Joe would be an offence punishable by up to six months in jail and a \$100 fine. "People should pay a price for their coffee that reflects the larger costs, like polluting water and cutting trees," Mr Young says. "Prices now are artificially low because they don't take into account all the externalities."



Basic coffee is trading at record low prices, averaging less than 50 cents per lb on the New York Coffee, Sugar, and Cocoa Exchange. Fair-trade coffees, by contrast, are selling at around \$1.25 per lb for regular and around \$1.40 per lb for certified organic beans. To receive fair-trade certification, coffee growers must be included in the International Fair Trade Coffee Register, which guarantees a "fair-trade price" and credit against future sales. Organic coffee is grown without pesticides, herbicides and fungicides, while "shade-grown" means grown under a canopy of trees, thereby protecting wildlife habitats.

Mr Young hopes to win voters on the strength of his environmental argument. Migratory birds which fly south to Central America each year, he points out, live in forests that are increasingly threatened by large-scale coffee growers, who cut down trees to replace shade-grown coffee with heartier new varieties that thrive in the open air. Moreover, the birds often return carrying pesticides, pollutants and fertilisers from non-organic plantations, potentially wreaking ecological havoc up north.

The denizens of Berkeley are used to paying a bit more for quality Java, and the idea of politically-correct coffee is not new. TransFair USA, the only organisation responsible for fair-trade certification in America, is based in neighbouring Oakland; and in 1999, Berkeley's mayor, Shirley Dean, sponsored a regulation stipulating that all coffee purchased by the city government must be fair-trade. Recently, though, she has expressed doubts about Mr Young's initiative, noting the enforcement difficulties if it is passed.

Coffee sellers, too, have mixed feelings. "He wants to make this punishable with six months in prison. I resent paying taxes for this kind of enforcement," says Ayal Amzel, owner of Yali's Café, near the university. "We have 13 people working here. We will be hurt. It will take a toll."

Despite the reaction of shopkeepers such as Mr Amzel (not to mention hate e-mails from across the country), Mr Young seems to have struck something of a chord. A subcommittee of the House International Relations Committee held discussions on the coffee crisis last month. Californian politicians have also weighed in. Congressman Sam Farr has recommended that individuals and institutional consumers purchase "sustainable" or fair-trade coffees. Pete Stark, another Democratic member of the House, has introduced a resolution that all branches of the federal government purchase only certified fair-trade coffees.

The Berkeley initiative may not pass this year. Nevertheless, the search has begun for what Thanksgiving Coffee of California, a leader in the gourmet coffee industry, refers to as "Not just a cup, but a just cup." ■

The Republicans and Iraq

A debate begins

WASHINGTON, DC

But it will remain a phoney war until the White House becomes involved

THE Republicans used to boast that they wanted a clear result in Iraq—regime change—but the Democrats only wanted a debate about it. Well, a debate of sorts has begun, and it is taking place largely on the Republican side.

It began on July 31st with hearings in the Senate Foreign Relations Committee. These provided a serious look at the issues. What weapons does Saddam Hussein have? What are his intentions? How solid is the opposition? Unfortunately, the testimony came from outside the administration—from think-tankers, defence experts and Iraqi scholars. These people all know a great deal about the technicalities, but they have no authority to take decisions.

The same point could be made about innumerable Pentagon leaks of possible war plans, which have filled newspapers this summer. These have revealed some sense of the scale of operations—anything up to 100,000 troops—and a sense of the caution of the joint chiefs of staff. Tommy Franks, the head of Central Command, this week said he is drawing up plans to give the president “credible options”. But that is all they are—options.

So when Brent Scowcroft, George Bush senior's national-security chief, wrote an article for the *Wall Street Journal* on August 15th called “Don't Attack Saddam”, it was the first sign of serious political debate. Mr Scowcroft argued that there was no real evidence tying the Iraqi dictator to terrorism. An attempt to overthrow him could destabilise the region and distract America from its real target, al-Qaeda.

Mr Scowcroft's broadside had echoes among mainstream Republican internationalists. A former secretary of state in the first Bush administration, Lawrence Eagleburger, concurred that Iraq was not necessarily public enemy number one. Senator Dick Lugar of Indiana chimed in: “Unless we plan this carefully, we're likely to destabilise other countries in the Middle East.” Chuck Hagel of Nebraska admitted that “Iraq is a threat”, but said that America has other interests: “Afghanistan...the Israeli-Palestinian issue...India-Pakistan”.

They stopped short of opposing an invasion outright—arguing it should be done carefully. Dick Armey, a congressman from Texas, was blunter. Mr Hussein, he said, has not shown “sufficient provocation” and “we Americans do not make unprovoked attacks.” Since Mr Armey is technically number two in the Republican

Party's congressional hierarchy (though he is retiring this year), this looked like a serious rift in party ranks.

Certainly the debate so far has shown a few things. It reflects some differences within the administration. But the debate among Mr Bush's people seems less about whether to remove Mr Hussein than about the importance of what happens next. It is mainly between those (like Paul Wolfowitz, the number two at Defence) who just want to see the back of him and those (like Colin Powell) who want to focus discussion on how Iraq ought to be governed after Mr Hussein's removal, and whether to postpone an attack until there is some

semblance of a government-in-readiness.

The debate also reflects a wider difference within the Republican Party. “Realists” want to get rid of Mr Hussein before he acquires nuclear weapons and destabilises the region. More ideological Reaganites want to get rid of Mr Hussein in order to destabilise the region—that is, to install a more democratic government in Iraq as a first step to changing autocratic regimes throughout the Middle East.

Reflecting such differences is one thing; but the debate so far hardly amounts to a serious split in the current Republican ranks. The most vocal dissenters are retired officials; and even their views need to be

American politics made easy

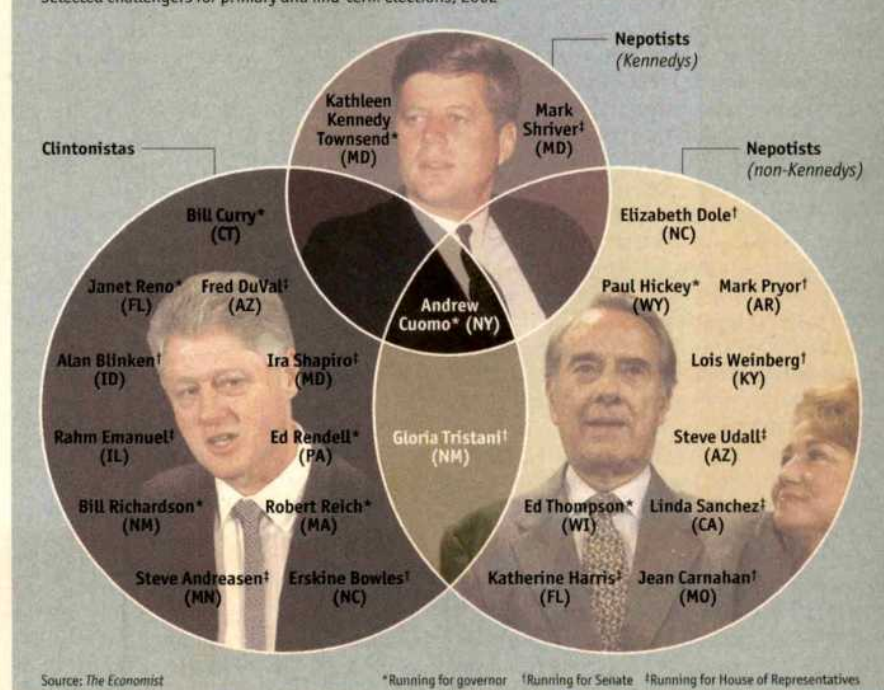
Who would want to run for election in America? Well, the incumbents have to, unless they want to start looking for another job. But that still leaves the wannabees: challengers who are prepared to devote money and time to races they will probably lose. What sort of masochists are they? As a courtesy to its American readers, *The Economist* presents this visual aid. For simplicity's sake (not to mention our reluctance to do research), all the candidates divide neatly into three categories:

- **Clintonistas.** Now that they have paid off their legal bills, most of Bill Clinton's cabinet and a slither of spin doctors seem convinced that if Hillary can do it, so can they.
- **Kennedys.** If you are a Kennedy who does not happen to be on trial for anything, you are expected to run, even if you are not called Kennedy. Kathleen Kennedy Townsend slyly uses feminism to get the brand across; her cousin, Mark Shriver, sadly cannot.
- **Other nepotists.** The Udalls of Arizona, the Pryors of Arkansas and the Hickeys of Wyoming are following the dynastic route. Elizabeth Dole and Jean Carnahan are copying their hubbies. Linda Sanchez wants the same job as her sister, Ed Thompson the same as his brother once held. Lois Weinberg is the daughter of a governor, Gloria Tristani the granddaughter of a senator (and a Clinton appointee to the FCC). The Bushes are focusing on defending Jeb, though Katherine Harris counts as an honorary family member.

And the perfect challenger? Andrew Cuomo, son of Governor Mario Cuomo, husband to a Kennedy and Mr Clinton's housing secretary—and on course to get clobbered either in the Democratic primary or by the incumbent, George Pataki. That's the spirit, my boy.

How to win votes and influence people

Selected challengers for primary and mid-term elections, 2002



Source: *The Economist*

*Running for governor †Running for Senate ‡Running for House of Representatives



Rice in the front line

► balanced, because some grand old internationalists support Mr Bush.

Writing in the *Washington Post*, Henry Kissinger, who probably carries more weight with the current administration than Mr Scowcroft, supported attacking Iraq. The erstwhile secretary of state admitted that few allies would support such an assault (something the *New York Times* seized upon with relish). But he disagreed with Mr Scowcroft's argument that it should be done only after calming down the Israeli-Palestinian conflict.

Another reason why the current debate feels like a phoney war is that it has not been partisan. With a couple of exceptions, everyone involved has been Republican. Few Democrats, with mid-term elections ten weeks away, want to distract themselves from domestic issues to engage in a national-security debate.

Lastly, the debate has hardly involved the White House. The closest it has got to overt participation was a much ballyhooed interview that Condoleezza Rice gave to the BBC, in which Mr Bush's national-security adviser ramped up the rhetoric by talking about "a very powerful moral case for regime change." But the administration has not been out in the public sphere much: it has neither responded to criticism nor explained itself in detail.

There are good reasons for this: an unwillingness to signal war plans; the risk of raising expectations too early. But other excuses seem peculiar—notably the idea that "we can't engage in a debate until after we've taken a decision." One result is that few of Mr Bush's critics, particularly outside America, have changed their minds. As Mr Kissinger admitted, "the president has made the intellectual case, he has not yet created the political framework." ■

Environmental disasters

The dead zone

ST PAUL, MINNESOTA, AND TERREBONNE PARISH, LOUISIANA

Aquatic life in the Gulf of Mexico is dying—and it is the mid-west's fault

IN 1973, Windell Curole was shrimping in the Gulf of Mexico with his father near the mouth of the Atchafalaya River, a tributary of the Mississippi. The river meets the salt water of the Gulf here to produce what has historically been the best shrimping grounds in the nation. After trawling for three hours, they hauled in their nets. "We came up with nothing," Mr Curole remembers.

What the Curoles had stumbled on is now known as the dead zone, a great swathe of Gulf waters that is completely devoid of life to about ten feet below the water's surface. Each spring, when algae bloom, they are poisoned by nitrogen and phosphorous that has been washed down by the Mississippi. The algae sink to the bottom where they are decomposed by bacteria. The bacteria use up the oxygen around them. Shrimp and fish and other mobile forms of aquatic life swim off in search of oxygen; the rest dies. The condition is called hypoxia.

The dead zone is yet another setback for Louisiana's beleaguered shrimpers and fishermen. Many have little understanding of the dead zone, beyond the empty nets they are pulling up, and having to travel further to find shrimp and fish. This summer, the dead zone expanded to some 8,500 square miles (22,000 square kilometres), an area the size of New Jersey.

Most scientists agree that run-off from mid-western farms is the main cause. Nitrogen fertiliser is relatively cheap, and farmers apply it liberally. The excess nitrogen runs off into the Mississippi. According to the Environmental Protection Agency, run-off accounts for 90% of the nitrates entering the Gulf: it also reckons that 56% of those nitrates flow into the Mississippi above the Ohio River.

Many farmers in the mid-west are aware of the problems they are causing. But they say they are trapped in a system which encourages the production of corn to the exclusion of other crops, which need less fertiliser. John Conzemius, a 69-year-old farmer, tends 160 acres of crops, including corn, in southern Minnesota, 12 miles from the Mississippi. Mr Conzemius says he would rather plant alfalfa, which can soak up nitrogen much better than corn. But no federal subsidies exist for alfalfa, so he plants corn instead.

Yet more farm-subsidies hardly seem a satisfactory answer. Another obvious solution—using less nitrogen—is opposed by farmers, because it would decrease yields.

Some scientists think that the nitrogen could be reduced by planting grasses to absorb the stuff before it leaves the farm. Another lot of proposed solutions involve tampering with the Mississippi itself.

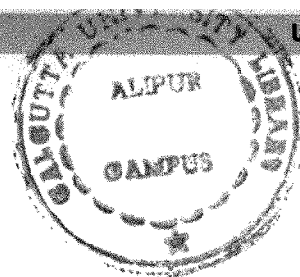
The government has long attempted to control the river by means of a vast system of levees. Nancy Rabalais of the Louisiana University Marine Consortium estimates that more diversions could reduce nutrient levels in the Mississippi by 5%. Unfortunately, such tinkering has dire environmental consequences of its own, such as increasing the magnitude of flooding, degrading wetlands and destroying wildlife habitats which might well offset any potential benefits to the dead zone.

Regulations are another option. Under the Clinton administration, a White House task-force drafted an action plan meant to reduce the size of the dead zone by 30% by 2015. The task-force, whose plan sets targets for reducing nitrogen run-off and also for restoring wetlands, continues to work under the Bush administration. For now, the plan remains voluntary. But if the dead zone continues to grow, the government could choose to make it law.

Shrimpers and farmers alike hope to come up with a solution themselves. To that end, a group called the Mississippi River Basin Alliance, along with the Corn Growers Association, brought shrimpers and fishermen together for a series of meetings in Louisiana and Minnesota in 1999. Shrimpers visited farms and farmers visited shrimp boats. "The farmers and the fishermen found out that their lives are parallel," says the alliance's director, Tim Sullivan. Their professions are equally disaster-prone and at the mercy of similar global economic forces. Perhaps that mutual understanding will help bring life back to the dead zone. ■



Lexington Behold the Rapture



Millenarianism is becoming a force on the right in American politics



THERE used to be bumper stickers in north Florida warning, "In case of Rapture, this car will be driverless." The Rapture is an apocalyptic event: at some point, Christ will swoop to earth and beam all true believers up to heaven. People will vanish, as the first book of Corinthians has it, in the twinkling of an eye, leaving everything else behind—the clothes they are wearing, their wedding rings, false teeth—and, of course, unbelievers. So if a car is being driven by a born-again Christian, it will careen off the road and crash into something. You have been warned.

To many people, particularly Europeans, the Rapture comes from the UFO-watching, conspiracy-obsessed fringes of American life, where "X-Files" enthusiasts meet the Montana Freemen to stockpile supplies in caves. Apart from marvelling at the varieties of religious experience, one's natural reaction to it is a Gallic shrug. Such things hardly merit political attention.

Not this year. Millenarianism—the belief in the thousand-year reign of King Jesus—is starting to spill out over its narrow banks and is flooding towards the mainstream. Conservative radio stations across the sunbelt have been full of this stuff since September 11th. But the best evidence comes from the phenomenon called the "Left Behind" series—a bestselling sequence of novels, whose sales have soared in the past year, that dramatise Americans' strange obsession with the end of the world.

The first book of the series (sales so far: 7m) opens under a slight cloud. Millions vanish overnight and Antichrist becomes secretary-general of the United Nations. From then on, it's all downhill. Antichrist, formerly the president of Romania for some reason, fools almost everyone "left behind" except a plucky band which includes, to Lexington's delight, a political reporter for an international news weekly. Antichrist engineers a peace treaty with Israel, institutes a world currency, rebuilds the Temple of Solomon, moves the UN to Iraq (don't ask) and persuades all nations to disarm. This is just asking for trouble. Volume five, "Apollyon" (3.1m sold), unleashes a plague of locusts with human heads and metal wings. Volume eight, "The Mark" (3m sold), has people queuing up to let Antichrist's world government implant micro-chips in their right hands—the mark of the beast. In the latest instalment, "The Remnant" (first print run: 2.75m), half of mankind has been killed or is living underground, the polar icecaps melt and the seas turn to blood.

"Armageddon" is due next spring.

Amongst the millenarian mayhem, "Left Behind" has a not-very-hidden political agenda. It is no accident, for example, that the poor old UN is Antichrist's chosen vehicle. International agencies and supra-national currencies are works of the devil. The kings of the earth "shall give their power and strength unto the beast" (Revelation 17:13). The whore of Babylon sits upon "seven mountains" (Revelation 17:9). Rome has seven hills. The Treaty of Rome is the European Union's founding charter. You can see where the authors are going with this.

The Book of Revelation is the source for the whole series. It was written soon after the fall of Jerusalem in 70AD and looks forward to a time when Jews will return to their homeland. In other words, to some Christians, the establishment of the state of Israel is intimately bound up with the Second Coming and the end of the world. The City of God is impossible without the state of Israel. This is a big reason why evangelical Christians are among Israel's most vociferous supporters in America.

If you combine these views with the spread of nuclear weapons—ie, things which actually could destroy the world—and the emergence of mega-terrorists bent on acquiring them, then it is not hard to imagine how the daily news can begin to look like front-line dispatches from the first stages of the end of all things. According to a poll by *Time* magazine, 59% of Americans think the Book of Revelation will come true. Almost a quarter believe the Bible predicted the attacks of September 11th.

This makes the "Left Behind" phenomenon fundamentally different from most millenarian cults. They tend to be marginal and isolated: David Koresh, who led his Branch Davidians into a fiery and fatal confrontation with the FBI, was a characteristic example. Readers of the "Left Behind" series are neither. The two most recent instalments both topped the bestseller lists. More than 40m copies have been sold in all.

Most of the series' readers surely voted for Mr Bush. Around the country, they provide foot soldiers for the Republican Party: they ring doorbells, stick envelopes and support their town's conservative radio station. They are the president's people. When Mr Bush talks about "the axis of evil", they take his phrase literally—and he knows it.

A date for your diary

Still, if the end of the world is nigh, policy of any kind seems rather pointless. Why bother? Walter Russell Mead of the Council on Foreign Relations explains why. Some views, he argues, are more dangerous to ignore than to contain. By talking in terms of the struggle of good against evil, Mr Bush is assuring millions of Americans that he is serious about defending them against terror; that he can be trusted to fight the good fight.

Foreign-policy sophisticates may despair at the uns subtlety of the president's rhetoric. They may despair even more at the beliefs of the end-of-the-worlders (many of whom would consign Mr Mead and the Council on Foreign Relations to the bottomless pit, alongside the Trilateral Commission and the European Union). But the critics are missing the wider—and real—danger. As McCarthyism showed, the demons of zealotry, once unleashed, can be devastating. Any American government—particularly a Republican one—thought to be failing in a war against terrorism could face forces far uglier than uns subtlety. To Mr Bush and his party, that may be a more serious worry than mere carping from abroad about lack of sophistication. ■



Corruption in Latin America

Waiting for the fat man to sing

Parliamentary immunity and American support have often let graft go unchecked. A case in Nicaragua suggests that may be changing

IT TOOK a revolution in 1979 to topple Nicaragua's Somoza dynasty of dictators, and then a decade of war before democracy was established. Now Nicaragua is in the throes of a less violent but equally momentous upheaval. At issue is the corruption that has oiled the political system no matter who ruled the country. Nicaragua's attorney-general has accused Arnoldo Aleman, the country's former president, and 13 associates, of looting \$96.7m before he left office earlier this year.

Whether or not Mr Aleman, now president of Nicaragua's National Assembly, faces trial will be a pointer to the outcome of the fight against corruption in Latin America as a whole. For although other scams in the region have involved more money, Nicaragua vies with Haiti as Latin America's poorest country, and depends on foreign aid. That makes the looting of its treasury especially repugnant. The missing funds are equal to 4% of GDP—or the whole health budget for a year.

A second reason why the case matters is that Mr Aleman, who took office in 1997, was a protégé of the United States in its 20-year battle against the left-wing Sandinists. From the Somozas to Peru's Alberto Fujimori and Argentina's Carlos Menem, the United States has had a habit of backing conservative strongmen in Latin America while turning a blind eye to allegations of their corruption. Now that policy may at last be changing.

Enrique Bolaños, Nicaragua's new president, seems determined to prosecute the case. That is a surprise. A colourless former businessman, he was Mr Aleman's vice-president and longtime friend. He was elected for the right-wing Liberal Constitutional Party, which Mr Aleman still heads. But Mr Bolaños made corruption an issue in his election campaign, and seems to make up in honesty what he lacks in charisma.

"Arnoldo, I never dreamed you would betray your people like this," he told a public meeting at which the attorney-general outlined the accusations against Mr Aleman. "You took pensions from the retirees, medicine from the sick, salaries from the teachers. You stole the people's trust."

The government claims that Mr Aleman and his associates laundered public funds through front companies and bank accounts in Panama, the Caribbean and Miami. They are alleged to have used thousands of official cheques to divert funds from government accounts, including those of the finance ministry and state-owned oil and communications companies. Mr Aleman is also alleged to have run up \$1.8m in personal expenses on a credit card charged to the Central Bank, including jewels, carpets, and bills for hotels and a Paris nightclub. Those accused include Mr Aleman's wife, a brother, a sister and a nephew, as well as three former ministers.

Mr Aleman has denied any wrongdoing.

ing. And some of the evidence is indeed confusing. It is unclear how much of the missing money can be legally accounted for. So far, Mr Aleman has been charged only with diverting about \$10m from the state television company to accounts in Panama. But other charges are likely. And fresh evidence is piling up.

The main obstacle to bringing Mr Aleman to justice is that he enjoys immunity from prosecution. A pact he made in 2000 with Daniel Ortega, the Sandinist leader, brought about constitutional changes that give both men automatic seats in the National Assembly. Mr Ortega invoked parliamentary immunity to avoid prosecution over claims that he sexually abused his step-daughter.

Blackmail over the budget

The government last week asked the assembly to lift Mr Aleman's immunity when it returns from its summer recess on September 10th. This requires only a simple majority vote. But Mr Aleman retains the support of his party, which has 53 of the 92 seats. He and his supporters have already blocked approval of the budget and tax reforms. Without these, Nicaragua will not qualify for further money from the IMF, and might have to default on its foreign debt. Nicaraguan officials have begun talks with the IMF over this impasse.

The government has the public on its side. Mr Aleman, known as "Gordoman" (Fatman) because of his physique and American links, left office despised. Nicaraguans have little to thank him for besides a few landscaped roundabouts from his period as mayor of Managua, the capital. Fast economic growth during his presidency came at the cost of swelling deficits, and did little to reduce poverty. Meanwhile, Mr Aleman declared assets of \$26,000 on becoming mayor in 1990, and ▶▶

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of \$1.4m on leaving office in 2001.

The United States also seems convinced by the case against him. Though not referring to Mr Aleman directly, American officials have repeatedly backed Mr Bolaños's anti-corruption efforts. Oliver Garza, the outgoing American ambassador, says the allegations amounted to "one of the biggest frauds committed in any country". He asks of Mr Aleman's allies in the National Assembly: "How much more proof do they want?"

Nicaraguan officials have hinted that Mr Aleman could be extradited for trial in the United States under American money-laundering laws. The State Department is following the case closely. The depart-

ment has revoked the American visa of Byron Jerez, Mr Aleman's alleged co-conspirator and former tax chief, now in jail in Nicaragua for his part in the alleged fraud.

Time may run out for Mr Aleman too. Mr Bolaños is threatening to organise a national demonstration against the assembly if it does not strip Mr Aleman of his immunity. Right across Latin America, parliamentary immunity has long been abused to prevent the corrupt from facing justice. This ruse is finally wearing thin. Brazil's Congress has recently expelled several members who faced corruption charges. Next month, Nicaragua's assembly could strike another blow against the impunity of the powerful. ■

goods worth ten pesos; now their value is around one peso, says Mr Pellioli.

Crime of other kinds is rising, too. Buenos Aires is plagued by thefts of telephone cables, manhole covers and ornamental plaques. Many posters are ripped down as soon as they are put up. Such goods are "recycled" by less scrupulous *cartoneros* than Mr Cordoba's team. The middle classes suffer "express" kidnappings, where a victim is taken for a few hours and released for as little as \$100. Another trick is more ingenious. Fake "market researchers", clipboards in hand, interview people in cinema queues, and obtain their name and address. They then contact their families, inform them that the victim has been kidnapped, and extract a ransom—all before the final credits roll.

Grim though life has become, Argentines show little sign of taking to the streets, to repeat the protests and looting that toppled two presidents in December. Their mood is one of depression and shame, more than anger, at the country's plight. No genuinely mass movement has emerged to articulate grievance. Street protestors from places like Lomas have little in common with well-heeled savers who gather outside banks to sing the national anthem while demanding that they be repaid their frozen bank deposits in dollars. Neighbourhood assemblies that sprang up during December's protests have degenerated into talking shops for bearded leftists nostalgic for the 1960s.

Officials claim that the economy's fall has finally halted. Last week, the government sent a draft letter of intent to the IMF; it hopes soon to have a limited agreement that would merely roll-over its debts to the Fund. But a new obstacle has arisen: Congress has approved two bills whose effect is to reverse the recent repeal of a bankruptcy law which favoured debtors at the expense of banks. With recovery still looking remote, the army of scavengers is likely to carry on growing. ■

Argentina's collapse

Sifting through the rubbish

BUENOS AIRES

The new poor are finding many ways to get by

OUTSIDE the office of the Nuevo Rumbo ("New Direction") recycling co-operative, a queue of women and teenagers forms in the wintry sun. They are waiting to be paid for their finds from a morning spent rummaging through the rubbish in Lomas de Zamora, a district of 800,000 people, on the outskirts of Buenos Aires. A couple of years ago, only a handful of *cartoneros*, as the scavengers are known, worked in the co-operative. Now there are more than 300 of them.

Since Argentina's economy collapsed at the end of last year, scavenging has become a mainstream job. Pepe Cordoba, the co-op's president, reckons that 15,000 families live from the district's rubbish, a five-fold increase from two years ago. In Argentina as a whole, he says, around 300,000 families are supported this way. Many of the new recruits once had jobs in the Buenos Aires' rustbelt, where miles of boarded-up factories testify to the demise of Argentina's industry. At least the devaluation of the peso since December has made Argentine rubbish competitive. Prices for waste cardboard, for example, are 20 times higher this year than last, Mr Cordoba says. A good *cartonero* can earn 600 pesos (\$169) a month, one-and-a-half times the average wage.

At the last official count, in May, 21.5% of Argentine workers were unemployed. In reality, says Artemio Lopez, a sociologist, at least one in three lacks a proper job. One in five citizens of what was long Latin America's richest country now live in extreme poverty, which according to Mr Lopez means they go hungry unless they have access to a free food programme.

The new poor have found new ways to make ends meet. Some have become *cartoneros*. Many have become streetsellers, crowding city centres. Others have dropped out of the money economy and rely on barter, through an exchange network that drew in as much as a third of the population at its peak earlier this year. Since then, around 30% of the network has closed down, according to Carlos Pellioli, who organises a barter market. It was swamped by a massive influx of people "who brought nothing but their hunger". As a result, it began to reveal some familiar Argentine vices. Extra credit slips were printed to accommodate the system's sudden growth. That, and counterfeiting, meant that the barter system has suffered hyperinflation. Ten credit slips used to buy



A growing and competitive industry



Politics in Canada

Chrétien's long goodbye

OTTAWA

The prime minister unveils his retirement plans, at last

TRUE to form, Jean Chrétien kept his Liberal party guessing right to the end. He had just made a tough speech to a party conclave, defending his leadership, setting out new policies, and taking barely veiled shots at Paul Martin, his chief rival, whom he fired as finance minister in June. But on August 21st, with the headlines in that morning's papers proclaiming "He'll stay and fight", Canada's prime minister of the past nine years suddenly announced that he would step down in February 2004.

Sudden it may have been, but not unexpected. Mr Chrétien's grip on power has been in question since his split with Mr Martin, who had refused to shut down his increasingly open campaign for the Liberal leadership. As a result, Mr Chrétien was likely to face, and to lose, a leadership vote at a party convention due next February. In an ill-advised move last week, his people asked all 170 Liberal MPs to sign a loyalty letter. Only 94 did so.

Mr Chrétien said that he hoped that his announcement would "end the fighting". Though for months he has teased questions about his intentions, he revealed that he and his wife had agreed two years ago that he would not fight a fourth election, and had quietly bought property in Ottawa. By February 2004, Mr Chrétien will be 70, and will have completed 40 years as an MP and ten consecutive years as prime minister—parliamentary milestones which he cherishes. He said he would also have implemented new policies to cut poverty, reform health care, and rebuild urban infrastructure. But a new leader would still have time to make a mark before the next election. This does

The Caribbean

Sick in Antigua

PORT OF SPAIN

The rot in a one-party, one-family, state

A SHOWER of cold water helped Antigua to come round after the excesses of its annual carnival this month. Following a year-long investigation into mismanagement of the Caribbean island's medical-benefits scheme, a Royal Commission of Inquiry recommended appointing a special prosecutor to look into charges against a dozen people, including two former health ministers, implicated in abusing the scheme. That ought to be an embarrassment for Lester Bird, the prime minister; if the man were capable of embarrassment, that is.

The report had been eagerly awaited. A sixth of the population of 72,000 had signed a petition calling for the inquiry. Islanders listened, riveted, to dramatic live broadcasts as 69 witnesses were interviewed. The scheme's former superintendent broke down as she gave evidence. Admitted to intensive care, she flew off to New York three days later. Two other witnesses were struck down with sudden illnesses. In May, the commissioners received a death threat, and there was a break-in at their offices.

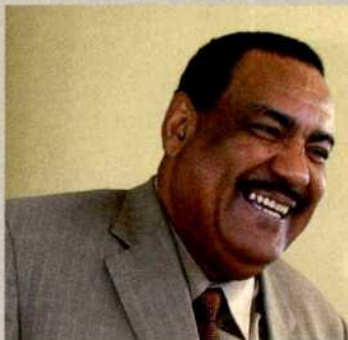
The commission found that the government had failed to pay in the contributions it had deducted from its own employees. Much of the money that did reach the scheme was diverted to the health ministry's budget, or spent on overpriced pharmaceuticals, and even a \$37,000 children's party. Though the fund provided patchy health care for most of the insured, it sent cabinet ministers abroad for annual check-ups.

The inquiry laid some blame on the scheme's auditors, Pannell Kerr Foster, concluding that a senior auditor in the firm's local office "designed and participated in a web of dishonesty to defraud

the [scheme]". But PKF claims that it warned of problems, could not be expected to look for fraud, and that the auditor concerned had an unauthorised private job with the scheme.

Antigua has other problems. A new hospital (partly funded by the medical-benefits scheme) that was not put out to tender is to cost \$60m, double the original estimate. Civil servants are routinely paid late. Widely-touted tourism projects have not materialised.

Mr Bird has been in office since 1994, having taken over from his long-serving father. His agriculture minister is his brother, even though an earlier inquiry into an arms-dealing scandal said that this sibling should be barred from public office. Nonetheless, Mr Bird is all insouciance. The inquiry made no direct criticism of him, and the offending ministers have gone. But as prime minister and finance minister, he makes the big decisions. He is balking at the commission's call to turn the scheme into an autonomous agency. An election is not due until 2004. Until then, hung-over Antiguanians had better avoid getting ill.



Not a cheep from Bird

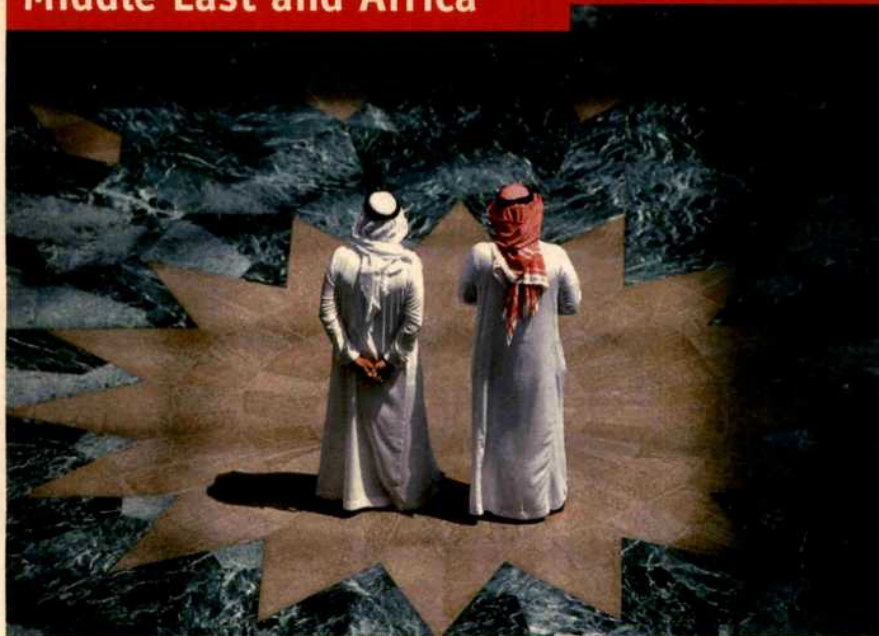
not have to occur before November 2005.

Far from ending the fighting, Mr Chrétien has made a clever attempt to control it. Despite Mr Martin's great popularity with Liberals, and across the country, Mr Chrétien seems determined to try to deny him the top job. By delaying his departure for so long, and by avoiding a straight fight with Mr Martin, he has tipped the odds against his former finance minister. Mr Martin will be 64 next week, and will be easily the oldest contender.

Mr Chrétien's apparent favourite is John Manley, his new finance minister, who will be just 54 when the prime minister steps down. Mr Chrétien said pointedly this week that "it will take possibly two

budgets of Mr Manley" to set the legislative framework for the new policies. By then, perhaps, Mr Martin's earlier successes in ending budget deficits will have been forgotten. Other contenders are also comparatively young. Sheila Copps, the heritage minister, will be only 51, and Allan Rock, the industry minister, 56.

Over the next 18 months, these younger cabinet hopefuls will have a chance to shine, while Mr Martin remains a backbencher in the shadows. But Mr Chrétien, a consummate political fighter, has lost his penultimate battle. By being forced to reveal his plans so early, he has consigned himself to a lengthy twilight in which to hobble around as a lame duck. ■



Saudi Arabian murmurs

Palpitations at the kingdom's heart

No revolution, but a burst of (relatively) open expression

SHOCKWAVES from last September's attacks on America continue to buffet Saudi Arabia, rocking its relations with the West and stirring change inside the kingdom. They have even reached Buraydah, a city famed for its rigid puritanism. Suddenly, in this desert Vatican, men are talking to women, even some with their faces bared, about reforming the strict Saudi branch of Islam. "We have to develop a modern, tolerant and inclusive interpretation of faith," says one of the participants, Mohsen al-Awaji, who was once jailed for religious extremism.

This is no revolution. Women still need permission from their male relatives to attend such meetings, and are not allowed to drive home. But the fallout could be far-reaching for Buraydah's clerics, who for the past 70 years have enforced their brand of Islam on the peninsula and used Saudi petrodollars to spread it throughout the world. In a town where television was long scorned, the guardians of tradition now compete to appear on satellite channels. One-time firebrands, such as Salman al-Awda, a dissident hardliner, issue cyber fatwas on the legality of anything from opening internet cafés to oral sex (both permitted, according to his website).

Nor is Buraydah just reassessing its relations with women. In the 1990s, a senior cleric pronounced the kingdom's underprivileged minority Shia sect to be pagans. Now Shia leaders are invited to give lec-

tures in the homes and on the websites of leading clergy, and on state television. There is a long way to go. The courts enforce a strict brand of Sunni law on all sects. But nobody, says a leading scholar, can now say that the Shia are not Muslim.

Outside Buraydah, old Saudi taboos are being regularly broken. In a society that bans the sexes from mixing in public, girls and boys in the Shia towns of the Eastern Province have braved riot police to march together for Palestine. In Jeddah, on the western coast, women staged their own rally along the Corniche. Young men shrug their shoulders at the religious police, the *mutawaeen*, who try to push them to prayer. Televised Lebanese soap-operas, sporting night-clubbing couples, attract larger audiences than the sheikhs, and popular web newspapers run by liberals use photos of scantily-clad Arab film starlets to pull the punters.

The *glasnost* has even infected the mainstream Saudi press. Earlier this year, newspapers attacked the hitherto untouchable religious police for killing 15 girls in a Mecca school dormitory. They had, said the press, prevented the girls' escape from a fire in the school because they were not properly veiled. In the subsequent outcry, editorials demanded and won an end to religious control of girls' education—no mean feat in a state where the clergy have held power with the Al Sauds for the past 250 years.

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Saudi old hands say that a few disgruntled people do not add up to regime-change. And they note that they have seen it before. After the last Gulf war, hundreds of liberals and Islamists risked prison to sign petitions demanding elections and accountable government. All they got was an unelected consultative assembly.

So, too, in response to the latest critical outbursts, editors known for their liberalism have been fired, and internet chat-rooms forced to close. Saudi eavesdroppers ensured that Mr al-Awaji, who had talked to *The Economist* by telephone, was banned from talking to the press, and deprived of his passport. And several of the petitioners on a manifesto, signed by 160 scholars, calling for a new attitude to non-Muslims, retracted their names after they were rebuked by Osama bin Laden sympathisers for showing more sympathy for the "collateral damage" of the attacks on New York than for the victims of the American bombing of Afghanistan.

But this time the protesters may not be so easily muzzled. After the Gulf war, the critics were bitterly divided, the House of Saud was strong and rich, and had unquestioned western backing. No longer.

Questions are being asked about how loyal young Saudis, who make up two-thirds of the population, are to a monarchy that in less than a generation has watched incomes fall from \$24,000 to \$7,000 a year. As King Fahd, aged 82, drifts in and out of hospital (he is currently resting in his Costa del Sol palace, having flown there with an accompanying fleet of private aircraft), there is disquiet over the eventual line of succession. Reformists discuss the formation of a new broad front.

Cracks in the alliance with America, which yawned open after September 11th, continue to widen. Leaked records from a Pentagon think-tank last month called the

► Saudi export of Islamic militancy "a kernel of evil", portraying it as a greater threat to America than Iraq. A group of bereaved Americans has filed a trillion-dollar lawsuit, accusing three senior Saudi princes, among others, of ultimate responsibility for the World Trade Centre attacks. Such projections of hostility, along with fears of over-zealous financial policing in search of terrorist funding, may have prompted Saudis to divest tens, perhaps hundreds, of billions of dollars in American assets.

Yet America's new punchiness, and its belligerence towards Iraq, could help the Saudi royal family in a backhanded way. Faced with a foreign threat, the kingdom is pulling together: Crown Prince Abdullah's refusal to let America use Saudi bases to strike Iraq is enormously popular. But this respite is likely to prove temporary: reform, eventually, is essential. ■

The Palestinians

Is it doomed?

BETHLEHEM

A plan to ease conditions in Gaza and Bethlehem stumbles into force

AFTER weeks of haggling, Israel and the Palestinian Authority (PA) agreed on August 18th to press ahead with the scheme called "Gaza, Bethlehem first". The brainchild of Binyamin Ben-Eliezer, Israel's defence minister, the plan has a modest goal: in return for Palestinian efforts to achieve a "ceasefire", Israel will relax its military and economic blockades in these two areas. If all goes well, similar arrangements can be extended to the six West Bank cities still under Israeli occupation. Hebron is marked as next in line.

In its first few days, the scheme has worked better in Bethlehem than in Gaza. On August 19th the army lifted the curfew on Bethlehem for the first time in 50 days, and withdrew its patrols to the outskirts, where a rigorous blockade was enforced. Uniformed Palestinian police officers emerged from the rubble of their offices to steer traffic, show willing and be welcomed by the city's 46,000 residents. "It's a step forward," said the mayor, Hanna Nasser, but pointed out that the siege still means an 80% unemployment rate.

In Gaza there was not even a step. On August 20th a Hamas sniper shot dead an Israeli soldier, in reprisal, the organisation said, for the killing of one of their men the week before. In return fire, the army killed a 15-year-old Palestinian, who was not the sniper. The next day Israeli tanks razed several houses, killing one Palestinian, in Gaza's Khan Yunis refugee camp.

And, Bethlehem apart, business was

much as usual in the West Bank too. On August 19th, a boy aged 13, who had been throwing stones at soldiers, was shot dead near Jenin. The next day, the army invaded Tulkarm refugee camp, killing an activist from Yasser Arafat's Fatah movement. The same day, in a shoot-out in Ramallah, an Israeli undercover squad killed Muhammad Saadat, the brother of Ahmad Saadat, who leads the Popular Front for the Liberation of Palestine (PFLP), and is held under American and British supervision in a Jericho prison. The PFLP vowed revenge.

It is not alone. All the Palestinian factions have come out against "Gaza, Bethlehem first", declaring it to be an Israeli ruse so that "there can be quiet in Bethlehem and curfews in Nablus." Their veto is crucial: no ceasefire can hold for long without active support from Fatah and at least tacit acceptance by Hamas. The Palestinian Authority has neither the strength nor the authority to impose order by force.

Why did Mr Arafat approve a scheme that seems doomed to failure? One reason is that by taking part, he hoped to refute Israel's claim that when it talked to the PA, it was not dealing with Mr Arafat. But the main reason, say Palestinians, was his lack of choice. He has been told, by the European Union and by Arab governments, that the only road to political and economic salvation is through local ceasefires coupled with genuine moves towards reforming his administration.

Military advisers from Egypt and Jordan are waiting in the wings to train the Palestinian police in ways laid down by the CIA. This week a PA delegation went to Paris to discuss institutional reforms with a group of American, EU and UN representatives. In return, says Ghassan Khatib, the PA's labour minister, the Palestinians seek economic help—and political pressure on Israel to lift the blockades. ■



Our own friendly policeman

Airwaves war

Towers of Babelaganda

CAIRO

Blasting out propaganda over the Middle East's airwaves

THERE is nothing new about trying to capture hearts and minds in the Middle East. It was to counter Nazi influence that the BBC launched its Arabic service in 1938, its first foray into foreign languages. During the 1950s, Britain and France accused Radio Cairo of spreading the virulent Arab nationalism that was damaging their imperial interests. But the region's airwaves have never been thicker with persuasion than now.

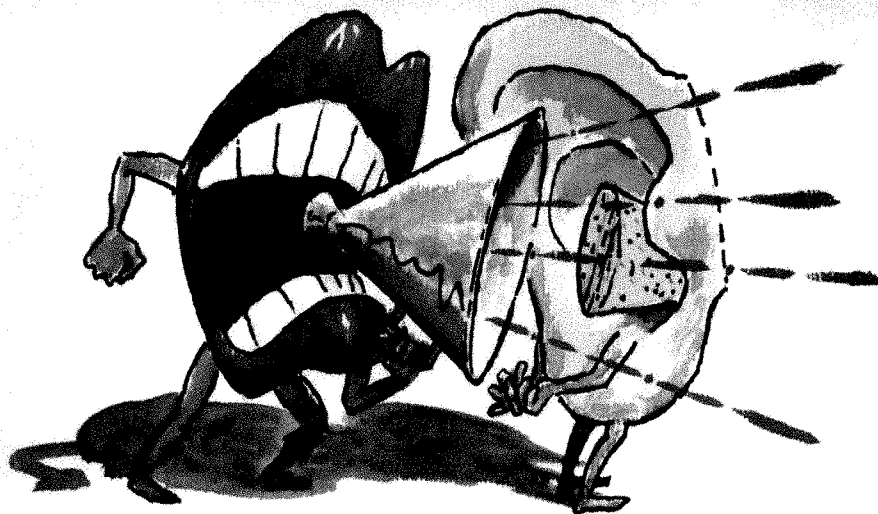
Since last September, the belief that "they only hate us because they don't know us" has gripped Middle Eastern policymakers. Oddly enough, the same idea has struck everyone at once. Americans blame hostile propaganda for the Arabs' failure to like their policies. Israelis say Arab "incitement" set off the *intifada* and still fuels it. Arabs and Muslims charge the western press with smearing and distorting their image.

Open mouths, closed ears

All are gearing up to meet the challenge, with similar prescriptions and, so far, similarly meagre results. Israel's new Arabic-language satellite television, for example, is hard to receive in Arab capitals since none of the government-owned Arab satellites that cover the region best will carry it. Arabs who do catch it may have trouble locating what Israeli newscasters describe as Judea and Samaria, or in identifying the Israel Defence Force, since these things are better known to them as the West Bank and the Israeli army of occupation.

Not that the counter-attack has been any more effective. Earlier this year, both Syria and Egypt started beaming Hebrew-language news programmes at Israel. Their intended audience finds the mix of quaintly academic Hebrew and turgid panegyrics for their countries' respective leaders comical at best. Iran has got into the act, too, broadcasting Hebrew news on short wave and the Internet. Even Hizbullah, the Shia militia in Lebanon, has plans to target Israeli airwaves. Its satellite television in Arabic is far slicker than state-controlled versions, but, when rendered in Hebrew, its exaltation of war, gore and martyrdom is more likely to disgust Israelis than win them over.

Arab countries are also seeking to spread their influence farther west. In June, after a year of deliberation, the Arab League pledged \$23m towards a media campaign against "Israeli and American ►►



► attempts to portray the Palestinian national struggle as unjustified terrorism". An English-language satellite channel is meant to be part of this effort, but bickering between the ministries of information that control most Arab broadcasting means it is unlikely to see the light of day.

Recognising this, a group of Saudi businessmen plans to sink \$160m into a private satellite television service targeted at audiences in Western Europe and America. To be known as ATV, the broadcaster will address what Prince Mansour Al-Saud, a nephew of King Fahd, describes as "the misconceptions and distortions of enemy stations" regarding Islam and Arabs.

America has opted for a slightly more original effort. Stung by the pervasive anti-Americanism in the region, and chastened by surveys showing that fewer than one in 50 Arabs ever listened to the Voice of America, the United States has scrapped its old Arabic service in favour of a souped-up model. Known as Radio Sawa ("together"), the service features Arab and western pop music, punctuated by brief news bulletins that highlight American achievements. The idea is first to hook the under-30s, who make up 65% of the Arab population, then slowly introduce more "information" content.

Norman Pattiz, a radio magnate who has championed Radio Sawa as a member of the government board that controls America's overseas broadcasting, promises to "deliver the audience for our diplomacy mission". So far, Congress has enthusiastically coughed up \$35m. Critics, however, dismiss the whole thing as "Pop-aganda", noting that the bitterest anti-Americans are hardly likely to be pop fans anyway. Although it was launched in March, the service can be heard on FM only in such safely Americanised havens as Kuwait, Amman and Dubai. The state broadcasting monopolies in places where America needs most to do better, such as Egypt, Syria and Saudi Arabia, are ultra-prickly about granting airwave access.

More to the point, Radio Sawa, like all its new rivals, will always be handicapped by an attitude that sees the fault lying with others. If everyone paused from blasting out words to listen, Americans might understand why they are seen as arrogant double-dealers, Israelis might realise why they are regarded as mean brutes, and Arabs might catch on that others have reason to find them xenophobic hypocrites. But that sounds like propaganda. ■

Africa expects...

To talk about jobs, not birds

JOHANNESBURG

What Africa wants from the summit on sustainable development

ASK the host of next week's UN summit on sustainable development what the gathered heads of state should be talking about, and you get a one-word answer: poverty. This, says Valli Moosa, South Africa's minister of the environment and one of the organisers of the meeting, will be the summit's theme. Without "concrete" or "pragmatic" action to fight poverty, fine words on greenery, global warming or fish stocks will come to naught.

To drive the theme home, Britain's prime minister, Tony Blair, will be whisked off to a rural village in Mozambique. America's secretary of state, Colin Powell, is to tour Angola, whose population is ranked the most wretched on earth by the UN. And, only five minutes' drive from the conference hall, delegates will be shown Alexandra township, one of South Africa's most stricken urban areas.

By concrete action Mr Moosa means measurable progress on the "millennium goals" of cutting illiteracy, infant mortality and poverty by 2015. Predetermined measurements can turn out to be unrealistic.

But the very fact that the conference is being held in Africa ensures that the region's problems will be to the fore. Some 14m people are facing severe food shortages; entrenched poverty and disease have sent life expectancy plummeting; sub-Saharan Africa is the world's poorest region; and southern Africa has the world's highest rate of AIDS infections.

At pre-summit talks in Bali and New York, delegates found it hard to agree on a text for debate, but all accepted that the focus should be on Africa. Thabo Mbeki, South Africa's president, has been asked to write about Africa's problems for the final declaration. His text will call on rich countries and multinationals to back Nepad, the South African-backed New Partnership for Africa's Development, by providing more aid and more investment.

The UN has tried to make Africa the centre of the summit's debate by proposing five themes that are thought to be especially important to the continent's recovery: water, energy, health, farming and biodiversity. The World Bank argues that agriculture should be kept as high as possible on the agenda, in order to attack the protectionist farming policies of the rich.

New UN projects, such as its Equator Initiative, which identifies 27 successful examples of development in the tropics, will be put on show at the summit. Says Sean Southey, who works for the initiative: "Even the negotiated text on bio-diversity will have a poverty focus. People ask if this summit is more about jobs or birds. It's jobs, so much more about jobs than the Rio meeting was ten years ago."

Even so, many Africans will be disappointed. AIDS campaigners from Botswana complained this week that the disease should have been the main focus. Representatives from UN agencies and the World Health Organisation privately concede that South Africa's controversial policy on AIDS means that the epidemic is being given less attention than it should be given, with roughly one-in-four sexually active southern Africans infected.

And, despite Africa's expectations, the conference in the end may provide more material on green issues and the changing climate than on poverty eradication. One lesson South Africa's government learnt from playing host to last year's disastrous UN summit on racism was that the best laid plans are sure to go awry.

For a start, and in the tradition set by Seattle, Washington, Prague and Genoa, Johannesburg's streets can be expected to be rowdy with anti-globalisation protest. The summit, say protesters, is a fraud, promoting heartless capitalism. Among the anti-privatisers, and fervent greens, will be members of South Africa's landless movements, fighting "rural apartheid". And Nepad, encompassing the "evils of neoliberalism" will be singled out for attack. ■

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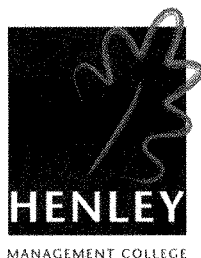
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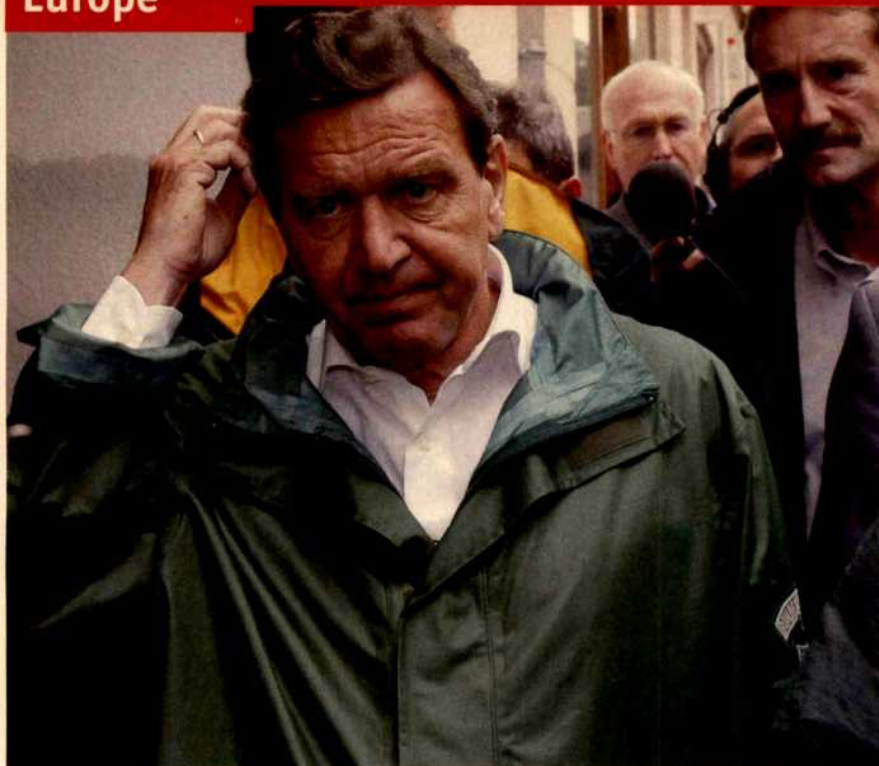
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The continent awash

After the deluge, moi?

FRANKFURT AND PRAGUE

The costs and political consequences of the great flood, especially for Germany and its chancellor, Gerhard Schröder (above), could be immense

THE newspapers and television call it *Jahrhundertflut*—the once-in-a-century flood. It has cost at least 16 German lives, swept away houses and cars, torn up roads, buckled railway lines and forced more than 100,000 to leave their homes, the biggest such evacuation of Germans since the second world war. The damage it has wrought in the former East Germany, still struggling to its feet a dozen years after the end of communism, has caused talk about a “second rebuilding” of the east and how to pay for it. And the flood might, just, carry Gerhard Schröder back into office as Germany’s chancellor.

There have also been casualties across the Czech Republic, where at least 12 people died. Some 210,000 were forced from their homes; several thousand lost them. Chemical plants seeped chlorine into the waters. A quarter of the farmland in Bohemia, the western part of the country, was swamped. The historic centre of Prague, the capital, was saved by a determined effort. But low-lying areas of the city suffered. Whole districts were under water, underground-train lines flooded, riverside restaurants and tennis clubs swept away. Pong the gorilla was presumed drowned when Prague’s zoo was submerged.

The president, Vaclav Havel, likened the mood of solidarity to the end of the Prague spring of 1968, when the Russians invaded. He now wants to reconsider how the Czech landscape is managed; some rivers, he says, were made more prone to flooding by communist meddling.

In Hungary, Danubian villages and suburbs upstream from Budapest were flooded too, but the banks on either side of the capital were, by a few feet, high and strong enough to keep the waters at bay. The mayor thanked the country’s ruling forefathers for their foresight in building such splendid defences. It is the Tisza river, the Danube’s tributary further east, that often does the flood-damage in Hungary. This time, though, it has held off.

But it is in Germany that the flood’s political and economic consequences may be most profound. The worst of the destruction has been in the eastern state of Saxony. The Elbe and Mulde rivers burst through towns and villages. Tame brooks turned into torrents. In the state capital, Dresden, the Elbe reached a record high on August 17th. People battled to save the baroque city centre (see next article).

As the Elbe’s floodwaters headed north, they left a terrible mess. More than

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530km (331miles) of railway lines in Saxony and 740km of roads were rendered useless and 180 bridges destroyed. The main rail lines connecting Dresden with Berlin, Leipzig and Prague were broken. Cars had been rammed against lamp-posts or through the surface of streets, the sides of houses ripped off. Countless shops and restaurants had been ruined. Streets and homes were caked in stinking mud.

Farther north, Germans braced themselves. Sandbags were filled and thousands of people evacuated from vulnerable spots. Fortunately, the weather stayed mainly dry, and, at midweek, a repeat of the upstream havoc looked unlikely, even though some places were flooded. The centre of Magdeburg, capital of Saxony-Anhalt, was spared as the river rose by less than feared. For all that, weakened dykes ➤



Floods and art

Treasures under water

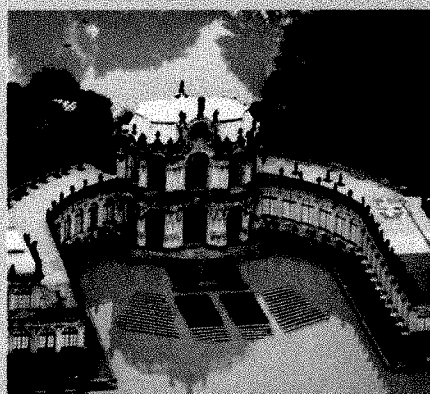
Despite heroic rescue missions, some great art has been damaged

IT MAY have been the swiftest salvage operation ever mounted to save a priceless collection, and must be counted one of the most successful. Last week museum staff, state-government officials, firemen, policemen and volunteers moved about 20,000 works of art in Dresden's galleries and museums upstairs, or to buildings they hoped were flood-proof. None of the art was destroyed, though some pictures and sculptures were damaged by the water or carelessness in the hasty move.

One of the most spectacular rescue efforts involved shifting 4,000 paintings from the Old Masters' gallery at the baroque Zwinger Palace in just seven hours during the night of August 13th. With electricity on the blink, helpers lugged an assortment of Rubenses, Rembrandts and van Dycks to the upper floors by torch and candlelight as the Elbe's waters kept rising. A few pictures were too big for the doors. Paolo Veronese's "The Rape of Europa", more than three metres wide, was one of five oversized paintings that were attached by ropes to the ceiling. They hang there still.

The Albertinum, a building on the banks of the Elbe housing four museums, opened its doors on August 20th for visitors to inspect the art-rescue mission. Yet it will take months if not years to repair the damage done. The workshops and tools that would normally be used to restore Dresden's art treasures have been swept away by the floods.

Meanwhile in Prague, another cultural treasure-house, officials at libraries, palaces and museums are coping with the worst flooding of the city since 1890. Some palaces close to the Vltava river were flooded. The cellars of the Jewish museum have been inundated; water



Dresden's beleaguered Zwinger Palace

rose to almost two metres in the Pinkas synagogue, the walls of which bear the names of 77,297 Czech victims of the Holocaust, and the nearby Old New synagogue. The contents of the famous national library at Charles University were saved, but many books were badly damaged by the damp.

Besides Prague, dozens of towns in the Czech Republic have also been badly hit by the floods. More than half of the historic centre of Cesky Krumlov was under water. A Renaissance city in southern Bohemia, Krumlov is one of the 730 sites on UNESCO's world-heritage list. In Pisek, another Bohemian town, one of the statues that adorn the oldest stone bridge in the country was swept away; the 13th-century bridge itself was badly damaged.

Lovers of the old and the beautiful are not the only ones to worry about the floods' toll. Ceske Budejovice and Plzen, two towns famous for beer sold under the cities' German names, Budweis and Pilsen, have been badly hit. No more brewing for the moment.

households insured against flooding has doubled since 1997, when Moravia, in the east of the country, was inundated. But it is still only one in five.

In Germany, Mr Schröder's handling of the floods may have revived his flagging chances of winning the general election on September 22nd. As the waters rose, the chancellor and his ministers sloshed around afflicted areas, being seen and promising aid. His conservative challenger, Edmund Stoiber, remained on holiday on a North Sea island. Only a few days later did he turn up on the Saxon dykes.

Walking on water?

Mr Schröder has looked decisive as well as sympathetic. On August 19th, he proposed postponing for a year income-tax cuts that are due to take effect at the start of 2003. This should raise €6.9 billion; another €1 billion has been found by shuffling the transport budget. On economic grounds this is questionable. No one knows how much money is needed, and it might have been better to raise it in another way—say, by deeper cuts in other public spending (the finance minister, Hans Eichel, has promised to find €250m in savings), or by issuing bonds and raising the necessary taxes over several years.

Politically, however, it looks spot-on. It smacks not only of firm leadership, but also of self-discipline: prodded by Mr Eichel, Mr Schröder is trying to keep Germany's swelling budget deficit below the 3% demanded of euro-zone members. There is even a hint of self-sacrifice: the tax reform is one of his proudest boasts.

Better still, Mr Schröder put the opposition in a fix. Because the tax cuts are already law, their reversal needs parliamentary approval. The conservatives could in theory block the plan in the upper house, which they control. Mr Stoiber has criticised the plan, saying that big businesses, which have already enjoyed the tax reform in the form of corporation-tax cuts, should also make a contribution.

Against that, Saxony, the prime beneficiary, is conservative-run; conservatives are also in government in other flood-hit states. And this is no time to look nit-picking. On August 21st the government said that it was willing to raise corporation tax, and thus rope in big firms, for the sake of compromise. The next day Mr Stoiber said he would not block the plan but would replace it with his own, using the Bundesbank's profits, if he won the election.

Much depends on whether Mr Schröder has genuinely impressed Germans with his handling of the crisis or merely done what they expect of those in charge. For several days, the dire state of the German economy, hitherto the dominant theme of the election, has scarcely been discussed. Mr Stoiber will be trying to ensure that the respite does not last. ■

- ▶ and the still-high level of the river meant that the danger had not yet passed.

The cost of all this is anybody's guess. Swiss Re, a reinsurer, has estimated €15 billion (\$14.7 billion) for the total damage done by the floods in Germany, Austria and the Czech Republic. Vladimír Špidla, the Czech prime minister, says the cost of cleaning up his country may exceed \$2 billion. Much of that will come from privatisation revenues and cuts in next year's budget. In Germany, the finance minister of Saxony on August 21st estimated the damage in his state alone would cost up to €16 billion (\$15.7 billion) to put right.

But many economists reckon that Ger-

many's GDP will scarcely be dented. Crops have been destroyed, it is true, and some people have not been able to get to work (or have no more work to go to), but much production will be delayed rather than lost altogether. Rebuilding work and the replacement of ruined goods may even give a bit of a boost to GDP.

Little of the damage in Germany, the Czech Republic and Austria will be covered by insurance—just 10-20%, says Swiss Re. Few Germans, especially in the west, want to insure against floods and those who do probably live in flood-prone areas where insurers charge high premiums. In the Czech Republic the proportion of

Germany's labour-market reforms

A plan to put Germans back into jobs

The conservatives have rubbished the Hartz commission's proposals—but if they win the coming general election they may well adopt a lot of them

THE greatest labour-market reform since the war", said the chancellor, Gerhard Schröder, as he endorsed the reforms unveiled by Peter Hartz, the Volkswagen personnel director who had been asked by the government earlier this year to write a blueprint to help tackle the country's painfully high unemployment. With a general election only a month away, the opposition has inevitably dismissed Mr Hartz's recommendations as a gimmick, too costly, and irrelevant to Germany's more pressing labour-market requirements. Mr Hartz said that his proposals, if acted upon, would create jobs for 2m of Germany's current mass of 4m unemployed, in three years. Wishful thinking, sniffed Edmund Stoiber, Mr Schröder's conservative rival for chancellor. The whole 343-page report, he said, was "rubbish".

The report does not deal with some of the most glaring causes of Germany's high unemployment, especially its exorbitant labour and social-security costs. But that, explains Mr Hartz, whose 15-strong commission included representatives of right and left, bosses and trade unions, was not its brief. It was set up in February after revelations that the Federal Labour Office had been grossly exaggerating its success in finding people jobs. With 181 regional offices, a staff of 90,000 and a budget of €54 billion (\$52 billion) a year, it clearly needed revamping. On that score, Mr Hartz has made some boldly innovative suggestions. Even if 500,000 Germans find jobs as a result, rather than Mr Hartz's hoped-for 2m, some €5 billion a year in benefits could be saved.

The German model to go British?

The commissioners took comparative soundings from half a dozen other European countries. Their aim is to bring the average length of unemployment suffered by jobless Germans down from the current 33 weeks to Britain's 22. Its planned new "job centres", replacing the old labour offices, are modelled on similar British centres, where each job-seeker has a personal case manager; staff who do well putting people into work get financial bonuses.

Though the commissioners do not suggest that out-of-work Germans should "sign on" every fortnight, as British job-seekers do, they propose new ways of pushing people into work. Within the job centres, "personal service agencies" (PSAs) will "employ" jobless people who have al-

ready been on the dole for an as-yet-unspecified period and hire them out to private companies as temporary workers. Those rejecting the offer of a job with their PSA would have their benefits docked. Restrictions on "temping" would be loosened. For the first six months, the wages of a PSA temp would be the same as his unemployment benefit; after that he would get the going trade-union rate for his type of work. The idea is to give jobless people some security, while letting the employer fire, and so hire, more freely.

One recent study suggests that only one in two of Germany's unemployed are actively looking for work. To change that, the Hartz commissioners at first wanted to reduce both the size of Germany's generous unemployed benefits and the length of time they can be dished out. At present, the unemployed get 60-67% of their previous net wage for up to 32 months, falling to 53-57% indefinitely afterwards. But opposition from Social Democrats, the trade unions and even the conservatives, who in Germany have traditionally been as keen on consensus, forced Mr Hartz to drop plans to change that. Still, the sanctions

that he does propose will, he hopes, provide a similar stick with which to goad the work-shy into jobs.

If the report passes rapidly into law, as Mr Schröder says it will (though not, for the most part, until after the election), all jobless Germans will have to register as unemployed as soon as they get notice of dismissal—or risk having their benefits docked. Job-seekers may be obliged to work for less pay than in their previous jobs, while young singles may have to travel anywhere within the country to take work. And it will be up to job-seekers to prove that a job is unsuitable, and not—as before—up to the labour office to persuade them that it is worth accepting.

On your bike, then

Critics say that much of this is beside the point, as there are too few jobs to go round. Not entirely so. Two-thirds of employers say they cannot get the staff they need; more than 1m vacancies are unfilled. Moreover, some of the commission's recommendations—encouraging temporary, short-term and part-time work, for instance—would indeed create jobs. So should the proposed domestic "mini-jobs", where earning up to €500 a month will be tax-free and subject to only 10% welfare contributions instead of the normal 22%. More questionable is a proposed "job floater" scheme, whereby employers in eastern Germany would get state-backed soft loans for hiring the jobless.

Getting people off the black market and into legal work is another Hartz proposal. The millions who work illegally are reckoned to turn over some €300 billion a year, roughly 15% of Germany's GDP. Many of them still take the dole. The commissioners suggest fat tax incentives to help them set up as a small company, described in the report as "Me plc" (Ich AG, in German), by filling in a single sheet of paper. Such workers could earn up to €25,000 a year, taxed at a nominal rate of 10%, while still getting unemployment benefit for up to three years, though they would have to pay welfare contributions.

Despite its recent broad condemnation of the proposals, the conservative opposition's reaction has been shifty. When the gist of Mr Hartz's ideas was first leaked in June, Lothar Späth, Mr Stoiber's designated super-minister for the economy, employment and eastern Germany, welcomed it as "revolutionary". Now, echoing his boss, he has changed his tune.

If the conservatives get in, expect a further, more nuanced, reaction. Many of Mr Hartz's ideas are in Mr Stoiber's own manifesto. Two-thirds of Germans say they would tip Germany "in the right direction". Mr Stoiber would surely put his own gloss on many of the proposals; it would be surprising if he did not, in the end, try to adopt many of them. ■



Hartz does his part-time job

The International Criminal Court

Choose your club,
America saysCentral Europe torn between the EU
and the United States

FOR the first decade or so after the downfall of communism, politicians in what was then deemed Eastern Europe breezily insisted that no choice need ever be made between friendships in the new world and the old. Since NATO and the European Union claimed to want roughly the same things—market economics, multi-party democracy, the rule of law—there seemed no reason to favour one club or the other.

Now the dilemma that the Central Europeans, as they prefer to be called, most feared may have arrived: they have been caught in the middle of a growing and ill-tempered dispute between the United States and the European Union, with each side issuing veiled threats to penalise any country that fails to do its bidding.

The row concerns the International Criminal Court, intended to try people for war crimes and genocide, which began functioning in The Hague last month. The EU considers this court a vital instrument of international law. In May it issued an "action plan", replete with four pages of arcane Euro-jargon, that committed EU countries to support and propagate the tribunal's work in every possible way.

The American administration, for its part, loathes the new court, does not accept its jurisdiction and is intensely concerned—obsessively so, some Europeans say—about the risk of American peacekeepers being unfairly victimised and hauled before judges in The Hague. It has asked each of its allies, including current and would-be members of NATO, to sign a waiver promising that Americans would not be extradited to the court.

So far Romania is the only European country to have done so. Mircea Geoana, its foreign minister, has explained that, as a former ambassador to Washington who knows American politics well, he never remembered coming under such pressure from the United States over a single issue. But his loyalty to Uncle Sam drew a stern rebuke from the EU.

Instead of yielding to America's salami-slicing tactics, present and future members of the Union were told by the EU's bigwigs in Brussels that they should wait, probably until mid-September, when the Union should have fashioned a collective response to America's forceful diplomacy. From the Romanians' point of view, however, it was well worth a reprimand from the Eurocrats: by pleasing the Americans over the court, they may well

have secured themselves a firm invitation to join NATO, along with six other countries, at the alliance's crucial summit in November in Prague.

Most of the other Central Europeans, including the instinctively pro-American Poles and Lithuanians, may well heed the warning from Brussels and avoid making a "separate peace" with America. Romania may have gone its own way because the EU, perhaps unwisely, has shown no enthusiasm for embracing it very soon.

What will the eventual pan-European response to America be? Britain, which has worries of its own about peacekeepers in distant war zones, could be pivotal; officials in London are hinting that it may be possible to grant the Americans the waiver they want without violating the new court's statute. British lawyers are poring over Article 98, which stipulates that "the court may not proceed with a request for surrender which would require the requested state to act inconsistently with international agreements."

The Germans and Scandinavians, notably punctilious in legal matters, are expected to hold out against any watering down of the court's statute. So expect quite a row within the EU in the next few weeks. If a compromise can be found, the Central Europeans will breathe a big sigh of relief. But it is unlikely to be the last transatlantic row in which Europe's newcomers become embroiled. ■

Russia and Chechnya

A calamity, yet no
end of war in sightThe biggest loss of life in a day shows
that Chechnya's war is far from over

VLADIMIR PUTIN, Russia's president, has often said that the "military phase" of his war against separatist Chechens is over. So it was a bitter blow to lose at least 115 soldiers on August 19th, when a giant Mi-26 helicopter plunged into a minefield near the republic's capital, Grozny. The chief prosecutor, Vladimir Ustinov, said a rebel attack was the "main theory" being probed after Russia's worst loss of life in a single day since Chechnya's conflict resumed in 1999.

But questions are being asked about possible negligence: why was the helicopter—which normally carries about 80 people—so heavily loaded? Inevitably, people are comparing the incident with the explosion on the Kursk submarine two years ago which took a similar toll, with official bungling and foot-dragging partly to blame.

As Russians held a day of mourning for the helicopter victims on August 22nd,



The military phase is over?

they looked back on a grim week. A day after the crash, an explosion in a Moscow building claimed eight lives and, though almost certainly accidental, instantly recalled the terrorist bombs that shook Moscow in 1999. The next day a liberal politician, Vladimir Golovlev, was shot dead in a Moscow street. Though there is no obvious link between the incidents, it seems to Muscovites that winter has come early.

Well before the helicopter crash, it was clear the Chechen war was flaring up, not cooling down. On August 15th, guerrillas attacked eight villages simultaneously. Their hit-and-run attacks have been killing a dozen soldiers a week. The rebel president, Aslan Maskhadov, last month signalled his will to fight on by naming an old rival, the fiery Shamil Basaev, to head his defence council. But the separatists, while retaining their ability to harass, are nowhere near to driving out the Russian security forces. The rebels have been depleted by years of war, and the taint of association with Islamic terror has drained world sympathy.

Nor can the fighters count any more on refuge in nearby Georgia. Russia has threatened to make incursions into Georgia's Pankisi Gorge, justifying them by the exaggerated claim that as many as 7,000 fighters may be holed up there. The Americans, who are due to start exercises with Georgia's ramshackle army next week, also want to stop Chechens crossing the border, if only to reduce tension between Russia and Georgia.

Why is Mr Maskhadov, a relative moderate, keen to battle on? Presumably to make the Russians accept that the price of endless war is too high. There are signs that Mr Putin, too, wants to change tack. In June he admitted that the situation in Chechnya was tragic. He may hope to do what the Soviet occupiers of Afghanistan attempted unsuccessfully—to entrench a "loyal" administration while the army pulls back. This time, such a strategy may have a fractionally better chance of working—if only because ordinary Chechens are so weary after eight years of war. ■

Charlemagne Pope John Paul II and the European Union

The pope didn't visit Poland to play politics, but he couldn't help it



THAT was some mass. A Polish pope conducting the office amid some 2.5m Poles genuflecting as far as the eye could see, at Blonia, the meadow in Krakow where in 1979 he had railed against communism and helped to speed its downfall. And in less obvious ways this was politics too.

It did not look like that. This was a homecoming, perhaps his last, for 82-year-old Karol Wojtyla. He was raised in a nearby town, was ordained into the priesthood in Krakow, then presided over the city as bishop and cardinal before getting the call to Rome in 1978 and emerging as John Paul II. Krakow was for him, he said, "the synthesis of everything Polish and Christian."

But for the 39m Poles John Paul II is more than a spiritual leader. While, even now, one Pole in two goes regularly to mass, four out of five say they try to follow the pope's example, and others quite outside the church admire him as a patriot. "I have to admit he was right about a lot of things," confessed Wojciech Jaruzelski, Poland's former communist boss. President Alexander Kwasniewski, an ex-communist agnostic, calls him "one of the most meritorious teachers of freedom in Polish history." Even the prime minister, Leszek Miller, who served in Poland's last communist politburo and has little time for Catholic smells and bells, was dutifully respectful.

So John Paul's homily at Blonia was required listening across Poland. In fern-green and gold vestments, his hands in spasm from Parkinson's disease, he spoke up for the poor, the unborn, and the terminally ill. But he said nothing at all about the European Union. And that was politics—and bad news for the government. Polish support for joining the EU is flagging and may well fall further still as the negotiators get into the last bone-crunching details with Brussels in the autumn. Well-informed Poles say there is a real chance next year's referendum on the issue could be lost. A clear message from the pope in favour of Poland joining would have carried weight. Blonia was the place for it. Most of those there were working-class people from the countryside; only one in six of the 7m Poles who go on a pilgrimage each year is a city-dweller. And these rural voters are just the ones the government needs to win over to the EU.

Messrs Kwasniewski and Miller failed to coax the words out of the pope. Limply, they re-emphasised his commitment to Poland's EU ambitions, which he had last outlined in a speech to

the Polish parliament in 1999. "We are strongly counting on his support in the next stage," Mr Kwasniewski said. The government's spin-doctors were desperate for any soundbite they could get. Instead, John Paul II denounced the "noisy propaganda of liberalism" which, he said, had cast many Poles into poverty since the collapse of communism. Andrzej Lepper, a firebrand farmers' leader whose populism appeals to Poland's underclass, jumped on this as proof that the pope, like him, is an anti-globalist. The League of Polish Families, a far-right party which fancies the EU to be a communist plot, crowed that it was just what they had been saying all along.

But then it is not the pope's business to satisfy politicians. In Poland, he spoke only glancingly on temporal matters. And he certainly knew just what he was—and was not—choosing to say. His performance over the four-day visit gave the lie to those who say he is no longer mentally capable. He was too frail to kneel down and kiss Polish soil or to light a votive candle at his parents' grave, but that did not stop him cogently evangelising.

He may also have been concerned for the unity of his church in Poland, which is not as solid as its present triumph might suggest. Again, the EU is at issue. Many priests, up to and including cardinals, are wary of it. "No one take this leaflet, it is propaganda," bellowed a priest from Lublin through a megaphone to his parishioners at Blonia, after having a pro-EU pamphlet thrust into his hand. The fervour at Blonia sprang from the charisma of John Paul II. But it had as much to do with nationalism, witness the patriotic anthems and flags, as with any new-found deepening of the faith. And the church has troubles weightier than divisions over the EU. Many Catholics in Poland as elsewhere reject Rome's teachings on divorce and even on abortion, let alone its lost war against contraception. The cardinal in charge of the Polish church, Jozef Glemp, is not hugely popular. And the church faces scandals as nasty as those in the United States. A Polish archbishop accused of molesting trainee priests has resigned.

The flight now leaving for Damascus...

In the end, the government got what it wanted. As he was boarding the jet back to Rome, the pope expressed the hope that the Polish nation would "find its due place in the structures of the European Union, and will not lose its identity but enrich the continent." Joining the EU, he said, would be a "positive aspiration" and a "courageous undertaking". John Paul II on the road to Damascus? No. He remains sceptical of the EU, Vatican diplomats say. He dislikes the free hand it seems to give member states on abortion, euthanasia or meddling with human genetics, and what he judges to be its materialist foundations. He would like to see an ecumenical religious element in the proposed new European constitution. And in another comment, though not in his set-piece oration at Blonia, he predicted that an EU which refused to acknowledge at least the possibility of a higher spiritual authority would collapse within a decade.

Politically, all that is unpersuasive: even if the EU were minded to aim for, let alone reach, harmony on matters of faith, it would be over temporal issues, such as farm policy, that its future might be imperilled. But the pope is not only thinking of what the EU could do for his country, but vice versa too. With its heavily Catholic population, Poland's influence in social affairs, he can reasonably hope, will be used in ways he would approve of; the church has a better chance of, say, saving unborn children with his beloved homeland inside the EU than outside. ■



Food and science

The grim reaper

The green lobby has won the GM debate, and the GM crop business is leaving Britain. Which, depending on your point of view, may be a good or a bad thing

IT WAS during his trip to India last year that Tony Blair was converted to genetic modification, according to Ian Gibson, chairman of the House of Commons select committee on science and technology. "The Indians were saying how delighted they were that Britain was having trouble with GM, because then they could take over and become masters of the science."

But Mr Blair's enthusiasm hasn't, so far, had much effect on attitudes in Britain towards GM. Last week there was another GM scare, when it turned out that Aventis, a Franco-German biotech company, had mixed in with a trial of an approved seed a small amount of a variety not approved for use in Britain. Never mind that this variety had been approved all over the rest of the developed world; the media went into its usual spin, talking of Frankenstein foods and Superweeds. The public mostly shares its concerns. According to MORI, a pollster, while 18% of Britons think the benefits of GM outweigh the risks, 39% think the risks outweigh the benefits, and the rest don't know.

That is why the government is launching a public debate next month, with a one-day summit, a public information film

and a lot of public meetings. Three years' worth of government-sponsored field trials of GM crops are to be evaluated next year, and the technology's supporters think that, although its opponents have made all the running so far, opinion can be turned around if the public is given enough decent information.

There are any number of theories as to why Britain, along with much of Western Europe, is so hostile to GM when America and most of the developing world are embracing the technology enthusiastically. Maybe it's because Britain is rich and small, and so its people are more concerned about their environment than are people in larger or poorer countries. Maybe it's because BSE has made the public deeply suspicious both of unfamiliar agricultural practices and of reassuring scientific pronouncements. Maybe it's because GM has become a totem for the anti-globalisation movement, which is stronger in Europe than in America. Maybe it's because organic farmers, an increasingly vociferous lobby which includes Prince Charles, have an interest in seeing off new technologies. Maybe it's because GM is a good excuse for keeping out foreign food.

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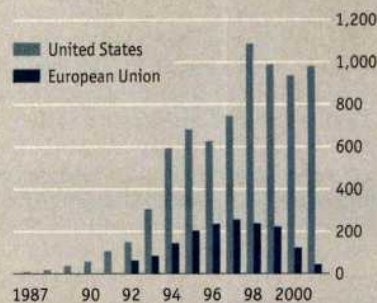
Maybe it's because Europe is right and America is wrong.

Whatever the reason, the consequences of the disparity are showing up. Outside Europe, GM is powering ahead. In 1996, no genetically modified crops were commercially cultivated in America. This year, around 34% of all maize, 71% of cotton and 75% of soya grown in America is GM. Canada, Australia, Argentina and China, among others, are also enthusiastic GM growers, and Indonesia and India have decided to go along with it too. No health risks have been identified, and evidence of the economic and environmental benefits is mounting: according to a paper on GM in China published earlier this year in *Science*, for instance, GM cotton cost three-quarters as much to grow per kilo as the conventional crop, and required only one-sixth as much pesticide.

In most of the European Union, there ►►

Withering in Europe

Field trials of genetically-modified plant species



Sources: European Union; Virginia Technical University

► has been a moratorium on commercial cultivation since Monsanto, an American biotechnology company, tried to launch GM products in the late 1990s and crashed against a wall of hostile public opinion. Research continues, but the economic and scientific consequences that India hopes for and Mr Blair fears are already showing up in research institutes and companies. The number of new GM products being developed in Europe has collapsed. In Britain, the number of field trials is down to four in 2002, from a peak of 37 in 1995.

This is particularly galling for British scientists, because Britain was second only to America in the development of plant biotechnology during the 1980s and early 1990s, and is losing its place to more enthusiastic countries such as China. According to Philip Stott, emeritus professor of biogeography at the University of London, these days there are somewhere between 100 and 130 transgenic scientists working in crop research institutes in Britain. The comparable figure for China is 1,988.

The decline of plant science in Britain is evident in both private and public sectors. Research and development capacity is shrinking. The number of crop-protection research centres has fallen over the past few years from six to one—the Jealott's Hill, Berkshire, research facility of Syngenta, a Swiss-British agricultural biotechnology firm. According to the UK Crop Protection Association, the number of R&D and technical jobs in the business fell from 2,400 to 1,638 between 1986 and 2000. These closures are the result of consolidation in the pharmaceuticals industry, not the consequence of the anti-GM campaign; but the campaign means that jobs in GM, the boom area in plant science, are not being created in Britain.

That is hardly surprising, given the climate. "Fieldwork in the UK is difficult now," says David Evans, head of research and technology at Syngenta. "Our trials are largely conducted outside the UK. We have had damage on our UK site. We had a stand of transgenic trees, which we were engineering to make them easier to pulp, so you could use fewer chemicals in the process. It was a four-year project. They were debarked. It had a disastrous effect on morale. There were tears."

The consequence of poor job prospects is being felt in the universities. "We're having big problems employing good graduates," says Chris Leaver, professor of plant science at Oxford University. "I've been in this business for 40 years, and I'm seriously depressed about the future of plant science in Britain."

Despite Mr Blair's enthusiasm, government support is declining too. "Funding for GM issues in horticulture has decreased significantly," says Brian Thomas, research director of crop improvement and biology at Horticulture Research Inter-

national, a government-funded institute. Scientists put that down to attitudes in the newly-created Department for the Environment, Food and Rural Affairs, where the green lobby, which has a friend in Michael Meacher, the environment minister, is said to have a louder voice than the scientists. "They wish there was no F in DEFRA," says another government scientist. "The department has turned tail on the whole GM thing." He estimates that there are 20-30 government-funded scientists working on GM horticulture now, half as many as there were five years ago.

Waste disposal

More rubbish

You can't bury it, burn it or recycle it. Getting rid of rubbish is getting harder

"WHERE there's muck there's brass," as they say. Well, these days, they're wrong. Growth, so devoutly desired by politicians and public alike, generates more and more rubbish. Getting rid of the stuff is more and more expensive, and there are no financial incentives to encourage consumers to cut back on waste.

Municipal waste—mainly generated by households—has been growing by 3% a year, broadly in line with the rate of economic growth. Britons currently dispose of about 30m tonnes of garbage a year.

Until now, Britain has opted for burying most of the stuff. Around four-fifths of municipal waste is sent to landfill sites. This approach has made considerable

It may be that next year's evaluation of the field trials vindicates the green lobby's objections. But whether it does or not, it looks as though the greens have won and agricultural biotechnology will continue to slip away from Britain. This should worry not just scientists and pharmaceutical companies, but also farmers and taxpayers. Farming in the rest of the world will continue to get more efficient, Europe will import more and more food and the burden of supporting Europe's farmers will increase. And there will, no doubt, be rejoicing in Delhi and Beijing. ■

sense in an island with sites to spare because of its particular geology and a history of quarrying.

But landfill sites are getting scarce, especially in southern England, where most people live. And they are becoming more expensive to run as the government insists on safeguards against environmental hazards like the leaching of toxic waste into underground aquifers. But the biggest constraint on dumping stuff in landfill sites is Britain's commitment to meet European targets to slash the amount of biodegradable waste—about 60% of household rubbish—that is put into landfill sites. These targets are intended to cut emissions of methane (a greenhouse gas) and to reduce ►►



What to do with current policies

The brown man of Europe

European recycling and composting rates*, 2001



Source: House of Commons

*Municipal waste

► the risk of water contamination from landfill. "European targets are the key driver," says Paul Frith of the Chartered Institution of Wastes Management.

If you can't bury it, an alternative is to burn it. This certainly seemed to be the initial thrust of government thinking during Labour's first term. A programme to build as many as 130 new incinerators was envisaged.

But burning also entails environmental risks. Although new incinerators are now much cleaner than previous ones, people are scared about exposure to dangerous chemicals like cancer-producing dioxins. The political difficulties in selling an expansion of incineration are immense. The government now appears to be backing away from incineration. Michael Meacher, the environment minister, expects that incineration will remain close to its current level of about 6-8% of waste disposal: "incineration remains extremely unpopular," he said recently.

If you have to bury less and you can't burn much more, another option is to recycle more. There's certainly ample scope to do this in Britain, which recycles (or composts) only about a tenth of municipal waste—far less than most European economies (see chart). The government wants to step up its recycling rate to 25% by 2005, an ambitious target. The Treasury is releasing £140m (\$214m) of extra funds to help local authorities finance more recycling.

Recycling appears to be a possible solution, but it can only work if there is demand for recycled materials. The market for recycled metals like aluminium works well, but this is not the case for other materials such as plastics. The government is investing £40m in a programme to find alternative uses for recycled materials and so to promote recycling. But recycling remains the most expensive option, which is why New York's mayor, Michael Bloomberg, announced last month that the city would give up recycling glass and plastic.

Church music

Discord

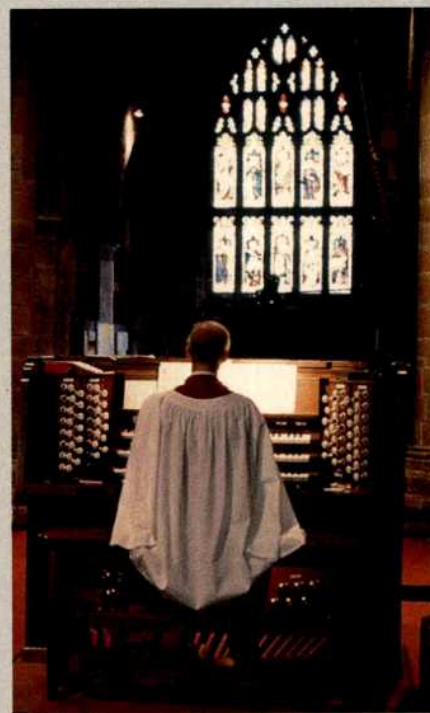
An unholy row in England's organ-lofts

COLIN WALSH has served as Lincoln Cathedral's organist and choirmaster since 1988. Last month, the cathedral chapter voted to abolish his job and replace it with the new post of director of music. Philip Marshall, Mr Walsh's predecessor, thinks officials are using "underhand methods" to dislodge one of Britain's finest musicians; the real problem, he says, is a personality clash with the precentor, the clergyman in charge of music. Protest letters are flying around; lay volunteers have resigned; Mr Walsh is taking legal advice.

Mr Walsh is not alone in his troubles. Church music, it seems, is becoming a hazardous profession. In the last few years, several other leading organists have been sacked or suspended from their posts; many more have moved abroad. In May, Ripon Cathedral's organist resigned; working with the dean, he said, had become too difficult. Dr Marshall complains that cathedrals have been taken over by "executives, administrators and pen-pushers", and music is often the first area to feel the squeeze. Many top organists, who make around £20,000 (\$30,000) a year, have been forced to take on heavy administrative duties; predictably, some have turned out to be hopeless managers.

John Ewington, general secretary of the Guild of Church Musicians, argues that the problems start in England's theological colleges, which he claims no longer give clergy a proper musical training. Parish churches, he maintains, are even worse off than cathedrals. Many local organists go unpaid, despite the high cost of lessons and music and the hours of practice they put in. Weddings, which used to be a nice little earner, are not the sure thing they once were. Even so, says Mr Ewington, the happy-clappy brigade often wants to run the whole show.

All this is hardly music to the ears of young musicians considering a career in the church; morale, says Simon Lindley, president of the Royal College of Organists, is running dangerously low. Happily, they may have found a champion in Rowan Williams, the next Archbishop of Canterbury, who was once a choir-boy himself. In a letter to a supporter of Mr Walsh's, Dr Williams says he wants to examine the status of organists under church law—they currently have none at all—and the funding of cathedral music. That may not save Mr Walsh's job, but it might stop some of England's aspiring church musicians from switching from Handel to hip hop.



Watch your back

The case for recycling rests on taking into account wider environmental benefits, such as cutting methane emissions when you reduce landfill.

Even if Britain does meet the government's recycling targets, a gap will remain between the growth in waste and a landfill capacity that will be increasingly constrained by the European targets. The obvious solution is to get households to throw less away. But this will happen only if households and consumers are made to pay directly (rather than indirectly through taxation) for the amount of waste that they

generate. Charges can also be used to create incentives for households to separate waste before collection, something that is vital if recycling is to become more cost-effective.

There was a political kerfuffle when a proposal to this effect by the Cabinet Office was leaked in July and the government appeared to back away from it. But plenty of European countries charge for collecting rubbish. It may be politically painful, but the only remaining alternative, incinerating the stuff, is likely to create even more of a stink. ■



High-tech companies

IT grows up

SAN FRANCISCO

While it waits for signs of a recovery, the information-technology industry is quietly maturing

WAITING for spending on information technology (IT) to pick up has become rather like waiting for Godot. Having grown by 16% in 2000, IT spending in the United States fell by 6% in 2001 and is expected to be stagnant this year (see chart 1). Analysts are fine-combing quarterly results for signs of a recovery. Last week brought some good news: Dell, a computer maker, announced a year-on-year increase in revenues of 11%. But the third-quarter results that HP, another computer giant, is to announce on August 27th will probably be less encouraging.

Hopes for a general bounceback in the second half of the year have long faded. Even optimists now say that recovery will not come before next spring. When it does, annual revenue-growth rates of 10-13% will be the best-case scenario, predicts Laura Conigliaro, an analyst with Goldman Sachs—half as much as during the bubble years.

In any case, focusing on an uncertain return of good old “new economy” times distracts from the fact that the IT business is undergoing profound changes. And most of these are likely to prove lasting.

Companies are not only spending much less on IT now, but they are also spending differently. Software vendors, in particular, can no longer depend on quick multi-million-dollar deals, but must work harder to win contracts that tend to be much smaller. More importantly, cus-

tomers' priorities have changed. Rather than buying e-business software or new computers, companies want gear that helps to cut costs, improve security and integrate existing software applications.

No surprise there, perhaps. In times of economic uncertainty, companies prefer small, short-term projects that fine-tune what they already have. The events of September 11th taught IT managers that they must make their systems more secure. And given big companies' current accounting woes, chief executives have gone back to spending more time with their chief financial officers than with their chief information officers—although they have not lost interest in technology, if a recent survey by Forrester Research is to be believed (see chart 2 on next page).

This new-found pragmatism is likely to prove lasting. In the 1990s, firms embraced technology religiously—first because they feared that the millennium bug might trigger an apocalypse, then because they were afraid of losing out in e-business. Now that such worries have faded, IT is just one of many tools that companies can use to stay competitive.

That realisation explains why technology investments now face the same kind of scrutiny as other forms of spending. Above all, they have to provide a clearly discernible return on investment. This also suggests that the IT industry—at least its more mature parts, such as hardware—is

becoming less of a “growth story” and more like a standard cyclical business.

Perhaps more worryingly for IT vendors, the industry is undergoing a shift in the balance of power between buyers and sellers. Again, it is hardly surprising that buyers currently have the upper hand in the market for computers and software. Nearly two-thirds of IT managers in America think that their ability to command better pricing terms is increasing, according to a survey published last month by Goldman Sachs.

But this change is merely the most visible part of a more profound trend. Traditionally, vendors have driven most big IT markets. They have been, for example, quite successful at locking in corporate customers. Once a company has deployed a piece of proprietary technology—say, an expensive package of enterprise software—it is very costly to switch to another provider. Software vendors can thus milk their “installed base” by selling them one upgrade after another.

IT buyers, however, are increasingly re- ➤

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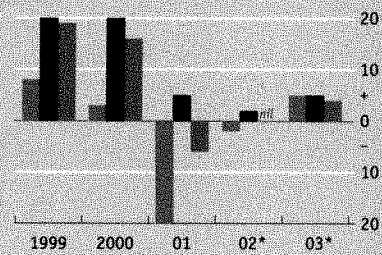
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Next year, maybe

US technology spending
% change from a year earlier

Computers and peripheral equipment
Services and outsourcing
Total technology spending



Source: Giga Information Group

*Forecast

luctant to play this one-sided game. They are putting pressure on vendors to make it easier for them to link the various bits of their systems. Indeed, the concept of collaborative e-commerce makes sense only if applications have a common language. What is more, vendors themselves increasingly favour open standards as a defensive strategy to neutralise the power of proprietary-minded competitors.

Being forced to do more with less, IT managers are coming to like Linux, the free operating system. Linux and the universe of "open-source" businesses that surround it are one of the few areas of the technology business that is actually growing. Almost a fifth of server computers sold by Dell now have Linux installed rather than Windows. Sun Microsystems has begun offering Linux servers, and might soon add a Linux PC to its product line.

If this trend towards openness continues, the IT industry will probably have to live with lower profit margins than in the past. Either way, argues Steven Milunovich, an analyst with Merrill Lynch, profits will shift away from hardware, which is becoming more and more commoditised, to software, services and consulting. IBM forecasts that these last three will account for 58% of industry profits in 2005, up from 42% in 2000.

All this will have a deep impact on the structure of the IT industry. Firms are following the money—or "moving up the stack", as technologists say. Sun Microsystems, which specialises in high-end server computers, is adding much more software to its product mix. And IBM recently bought the consulting arm of PricewaterhouseCoopers, an accounting firm.

What is more, the big are likely to get bigger. These days, customers prefer buying from well-established vendors with integrated offerings, such as Cisco, the leading maker of networking gear. Being the most efficient vendor, Dell is also gaining market share—hence its good results.

The merger of Compaq and HP, two leading computer makers, is only the beginning of consolidation in hardware. Andrew Neff, an analyst with Bear Stearns, even predicts that, to combat IBM's growing power, Dell, Sun and EMC could forge tighter bonds. So far, there have been few post-bubble mergers and acquisitions, partly because targets consider their shares undervalued—and few are as indebted as their telecoms peers. There are roughly twice as many high-tech companies today as there were in 1995, and only around a third of them are profitable, according to Merrill Lynch.

It does not follow from this, however, that technology itself will come in larger chunks. Because companies increasingly

want to buy modest IT solutions that can be expanded as and when the company outgrows them, the technology vendors that prosper are likely to be those offering "modular" products that can be installed one part at a time.

So will the IT industry in future consist of giants that innovate only incrementally, just like the leading companies in mature industries, such as cars or chemicals? That is unlikely. Shocked by the severity of the technology recession, IT companies are maturing quickly. But technology has a way of surprising the world. It may not be long before some proverbial teenager in a garage invents the next killer application, and gives the industry back at least some of its legendary buzz. ■

Softbank

Setting Son

TOKYO

Japan's Mr Internet has struggled to put his house in order

SADLY, the bad news may not be bad enough. Masayoshi Son, the Japanese entrepreneur who personifies that country's Internet sector, suffered another blow last week when America's Nasdaq pulled the plug on the Nasdaq Japan stockmarket, a joint venture in which Mr Son's Softbank owns a 43% stake. Softbank can easily afford to write off its ¥1.2 billion (\$10m) investment in the two-year-old market; and Japan's handful of tradable tech firms can find other places to list their little-known shares. The more troubling question now is whether the latest failure will prod Mr Son to take a hard look at his fragmented technology empire—before he fritters away the rest of it.

When the technology bubble inflated, Japanese tech shares managed to capture some of the hot air. But unlike in America, where scores of over-rated executives gained fame and riches, Japan's Internet boom-and-bust became indistinguishable from the fortunes of just one man: Mr Son. Indeed, even at the end of 2000, after the bubble had burst and Softbank had lost 90% of its value, *Forbes Global* magazine was still kind enough to name Mr Son its businessman of the year, on the grounds that trillions of yen in paper losses could not outweigh his role as matchmaker between Japan and cyberspace.

Despite Mr Son's frenetic activity on the home front, however, Softbank has made most of its fortune from a few well-placed punts on shares in foreign technology firms. Two of these account for the bulk of his ¥480 billion in unrealised equity gains: Yahoo, an Internet portal; and UT

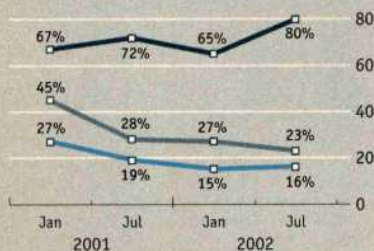


Son takes questions, and there are many

Playing it safe

"How well does this statement describe your company?", % answering yes

- Our executives are enthusiastic users of information technology
- My company is willing to experiment with new, unproven technologies
- My company is willing to buy and roll out technology from start-ups



Source: Decision-makers from 3,500 global companies

Starcom, a telecoms business with big investments in China. Yet rather than simply pocketing the cash from these bets, Mr Son has tried to parlay his winnings into an integrated media, Internet and telecoms giant. Together with this full-service Japanese technology conglomerate, he has pursued a scatter-gun approach to venture capital: one of his self-confessed goals has been to help start as many new companies as possible in the hope that some would succeed.

Although Nasdaq Japan's collapse will not by itself undermine the smaller firms in Mr Son's portfolio, it calls attention yet again to the flaws in the venture-capital side of Softbank's business. The original idea behind the new market was to help

Making diamonds from cremated remains

Stones from bones

ELK GROVE VILLAGE, ILLINOIS

For \$4,000 you can now wear a loved one on your finger

THE next time someone tells you that diamonds are a girl's best friend, they may not be speaking metaphorically. Those sparkling gems may really be her best friend, or her husband, or even her dog. Life Gem, a small company based near Chicago, has started offering diamonds made from the cremated remains of people and pets. Funeral homes in Illinois, Wisconsin and New York have signed up to market the service to their clients, who can literally have loved ones wrapped around their fingers for eternity.

Life Gem estimates that the carbon from one cremated human body can yield up to 50 stones of varying sizes. With prices starting at \$4,000 for a quarter-carat, though, it will not be cheap to add Uncle Harold to the family's jewelry collection.

Although the idea may sound weird, the company insists that it is technically feasible. According to Life Gem executives, an American-owned diamond laboratory in Germany spent three years developing the process of extracting carbon from animal and human bone; turning it into precious stones is the easy bit. The lab's anonymous owner will reportedly produce stones for Life Gem until the company builds its own facility in America.

It may be on to something. A growing



"It's what they would have wanted"

number of Americans—about a quarter of those who died last year—are cremated. Life Gem says it is also looking to Japan, where the vast majority of people are cremated, and to the pet market for more opportunities. And if these new markets do not suffice? It could always start competing head to head with Atlanta-based Eternal Reefs, which mixes ashes with concrete and uses the blocks—a "permanent environmental tribute to life"—as coastal reef formations.

This manoeuvre was something of an eye-catcher, even by the standards of recent corporate shenanigans in America. Ben Wedmore, an analyst at HSBC Securities and a tireless Softbank critic, summed it up as "a takeover bid of [Softbank's] own company on its own exchange. It had sort of a 19th-century feel to it."

Realistically, Mr Son's only bridge to the 21st century is Yahoo Japan, a domestic portal he has built with the help of the American firm. However, instead of simply building up the portal service, Mr Son has also tried to erect a broadband network, through yet another subsidiary, with which to lure more Japanese online. The few analysts who still bother to follow Softbank reckon this is a mistake. The company does not have a convincing strategy for taking on NTT, Japan's dominant telecoms carrier. Moreover, the broadband business's cash is being used to subsidise Yahoo Japan. Unless Mr Son puts an end to such practices, increases Softbank's focus and straightens out its balance sheet, he can expect plenty more failures. ■

Cable manufacturers

Nifty twisters

LYONS AND MILAN

The Europeans stay ahead in a capital-intensive industry

EUROPE has lost plenty of industries to low-cost competitors, many of them from Asia. But it has clung on to a leading position in the global market for cables—the wires that carry electricity, Internet traffic or telephone calls—despite the existence of well-established Asian rivals. Sumitomo Electric, the world's third-biggest cable maker, was founded roughly 105 years ago. But it is yet to catch up with Nexans, spun off last year from Alcatel, a French telecoms-equipment manufacturer, and the cables division of Pirelli, an Italian industrial group best known for its tyres (see chart on next page).

The overriding reason why these Europeans have been able to fend off Asian rivals is that around 70% of cable production costs are raw materials, mostly copper, which cost the same the world over. Labour accounts for a mere 10% of overall costs. As a result, Europe's producers are all but immune to Asia's biggest advantage: its lower labour costs.

The cable-making business is a demanding one and many companies are struggling. There are three long-term reasons for today's difficulties. The first is that consolidation among telecoms and energy companies has put pressure on prices, as big customers have asserted buying power. A second factor is the current telecoms slump, which has knocked the stuffing out of the previously lucrative market for fibre-optic cables. On top of this comes a capacity hangover from German unification in the early 1990s, when cable makers ramped up production so that infrastructure in eastern Germany could be quickly improved.

Cable makers have responded to relentless pressure from customers for lower prices by innovating. Europe has long led the way in cable technology, thanks to companies such as Câbles de Lyon in France (now Nexans), BICC in Britain and Pirelli. Lyons remains an important site for Nexans, both for its new research centre and a highly flexible manufacturing plant that can produce more than 2,500 different types of cable.

Both Nexans and Pirelli have invested heavily in research and development. Nexans, for example, has more than 500 patents. Research ranges from the pursuit of advanced new polymers as covering for cables, to engineering that makes production systems cheaper. Both Nexans and Pirelli also do research into fibre-optic tech- ➤

► make initial public offerings more popular in Japan. That would benefit Softbank, by allowing it to cash in on its hundreds of investments in tech firms. The trouble is that, unlike true venture capitalists in America and elsewhere, Mr Son has done little to add real value to the firms in his stable.

Consider Club ir, one of the few firms that Mr Son has already managed to list on Nasdaq Japan. When it teamed up with Rupert Murdoch to launch a Japanese satellite broadcaster, now called SKY Perfect, Softbank set up Club ir through a subsidiary in order to "market" SKY Perfect's subscriptions. The effect was to hive off to the new company the costs of building SKY Perfect's customer base—a move that disillusioned telecoms and energy investors in America will no doubt appreciate. In March this year, Softbank took Club ir public on Nasdaq Japan. A month later, SKY Perfect cancelled the firm's contract, sending its shares down. Mr Son then had to clean up the mess by having Softbank buy back Club ir's shares at the original listing price, swallowing all of the losses.

nologies, the former to plug a gap caused by Alcatel's decision to keep its fibre business when it spun off its other cable operations to Nexans.

Although the Europeans are clear leaders, the global cables market remains fragmented. Gérard Hauser, chief executive of Nexans, reckons the top ten cable makers account for no more than 25% of the industry's roughly €80 billion (\$78 billion) of annual sales. For every big firm there are dozens of small, specialist competitors. Take the production of basic electric cable. Italy alone boasts around 250 producers, Europe more than 4,000. China, a growth market, has around 2,000 makers of energy cables.

Although there is no shortage of companies for sale, consolidation is unlikely to happen quickly. One reason is that companies fear repeating past mistakes. Pirelli has struggled in recent years to integrate both BICC and the cables arm of Germany's Siemens. Pirelli took on big debts to buy these rivals, but found it hard to restructure their far-flung operations. Pirelli put its energy-cables business up for sale last year, but failed to find a buyer and is now trying to restore the unit to health.

Mr Hauser says there is scope for mergers, pointing to America as a particularly promising market for deals. With or without consolidation, cable makers face a

tough environment. Nexans operates with one-third fewer factories than it owned four years ago and has shed almost 6,000 jobs, or roughly a quarter of its workforce.

Against such a grim background, Europe's big producers can thank a series of lucky breaks for their relative prosperity. Pirelli, for instance, sold its fibre-optic components arm in 2000 at the top of the fibre-optic boom, raising \$3.6 billion in cash from Corning, an American rival. Had it not had that good fortune, it might have faced nastier options for its troubled energy-cables business.

Face-to-face communications

Press the flesh, not the keyboard

In a wired world, physical presence counts more than ever

AS A young man in the City of London, recalls Sir Martin Sorrell, boss of WPP, a marketing group, he was struck by the magnificence of the partners' room at Hambro's. The bank's top brass sat in a vast hall above Bishopsgate, surrounded by their aides. "There was a lot of noise," he says, "but everybody knew what everyone else was doing."

The newish mayor of New York, Michael Bloomberg, began his working life as a trader for Salomon Brothers, and has recreated something similar in his office in City Hall. Officials work in cubicles within a giant, open bull-pen, rather than in private offices. Again, the aim is to free the flow of information. The inevitable conclusion: seeing other people in the flesh is a different, and sometimes better, way to make sure that news and views flow freely than anything that electronics can offer.

One of the mysteries of the wired (and wireless) world is that proximity still counts. In spite of September 11th, and the predictions that everyone would travel less and have fewer meetings, people still want to gather to do deals, to drum up new ideas and to court customers. Indeed, in some ways, physical presence counts even more than it used to. Tony Venables, an economist at the London School of Economics, believes that businesses that thrive on face-to-face communications—or what some call F2F—now account for a growing share of economic activity.

Of course, the arrival of the Internet and of cheap long-distance telecommunications means that lots of activities that once required physical presence can now be conducted online. Customers can pay a bill, book a hotel room or place a bet without walking to the bank, travel agent or bookie. The fall in the costs of undertaking

Nexans was doubly lucky that Alcatel chose to retain its fibre business. As a consequence, Nexans not only has limited exposure to the collapsed telecoms market, but also has a strong position in copper telecoms cables, a subject of renewed interest among telecoms companies keen to find new uses for traditional cables. Better still, a stockmarket flotation last year left Nexans with a debt-free balance sheet, a rarity among big companies in capital-intensive industries. That should allow the world's biggest cable maker to retain its lead for a while yet. ■

such routine transactions has allowed companies to move them out of expensive city centres to cheaper locations.

But other kinds of business seem to need proximity more, not less, these days. Look at the way the venture capitalists who financed the Internet boom huddled together along Sand Hill Road in Palo Alto; or the clustering of media folk along New York's Avenue of the Americas. "If you are doing a multi-million-pound deal, you need to eyeball them," says Dame Judith Mayhew, chairman of the policy committee of the Corporation of London. "You don't do that down the line."

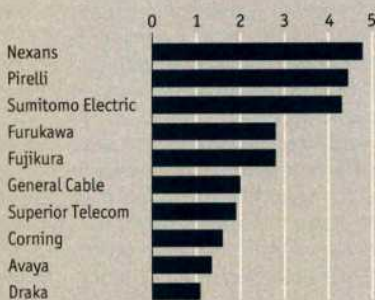
Cities are still highly efficient ways to ensure that eyeballers can see each other. Some trades seem to thrive on density. In a paper recently published by the National Bureau of Economic Research, Sukkoo Kim points out that 40% of American employment is packed into 1.5% of its land area. Those cities that specialise in some services—notably finance, insurance, property dealing and wholesale trade—have tended to pack more and more workers on to the same land, he argues, unlike those that specialise in services such as public administration or retailing.

Why might that be true? Michael Storper of the University of California, Los Angeles, has written a paper with Mr Venables on "Buzz: The Economic Force of the City". They argue that cities are where information and ideas are developed and swapped. But not all information is equal. Some (a bank statement, say, or a booking) is easily codified and electronically swapped; while some ("I have a deal for you", "why don't we do it this way?") requires context and trust to be meaningful. It is the second kind of information that requires F2F.



Keeping the Asians at bay

World's biggest companies by cable sales, 2000, €bn



Source: ABN Amro



Keep it under your hat

As a result, many activities are bifurcating. Hollywood film-shooting is continuing to move out of town, for instance, while deal-making, which requires trust and lots of parties, stays in town. And this split does not apply merely to the movie world. Much American manufacturing is going to small and mid-sized cities inland. A typical beneficiary is Memphis, where Federal Express has its hub. The deal-making and design tends to remain in the big cities of the two coasts.

For individual companies, the key question is when and how to bring people together. Companies with lots of outlets need to keep branch staff in touch with head-office staff. One company that works hard at this is Wal-Mart. The retailer's founder, Sam Walton, spent much of his time tramping round the company's stores. Nowadays, regional and district managers spend four days a week on the road, listening to what store workers are saying.

Even a company such as Oracle, which tries to do as much as possible electronically, finds that it needs regular face-to-face contact. Jim Flynn, its head of corporate communications, brings his regional staff together once a quarter. "It's the only way to work through complicated co-ordination issues," he says. Moreover, in a global business with different national thresholds for irony and humour, and with English widely spoken as a second language, the Internet can breed misunderstandings if not backed up with regular meetings.

For companies whose lifeblood is creativity, personal contact matters even more. Silicon Valley was born from long nights spent drinking in the now-defunct Wagon Wheel bar in Mountain View, California, where the early geeks and semiconductor executives thrashed out technical glitches together over beers. Big pharmaceutical companies struggle to build into their bureaucracies the sparky communal brainstorming that creates breakthroughs. According to Louise Red-

mond, head of organisation effectiveness at GlaxoSmithKline (GSK), recent meetings of staff from around the world have revealed gaps in research programmes that would otherwise have gone unnoticed. She says that GSK has increasingly tried to cluster teams working on a particular project on the same physical site.

The need to put the right people together also feeds into office design. At WPP, Sir Martin says, "we're blowing out walls and creating coffee areas." No longer are accountants and media people assigned to separate floors. Instead, they work side by side in teams to ensure that they keep talking to each other.

Advertising gaffes

Sticky issue

What possessed Cadbury-Schweppes to liken its chocolate to Kashmir?

HERE'S a first: a politically incorrect chocolate bar. The Indian division of Cadbury-Schweppes, a venerable confectionery company, has incensed large swathes of Hindu society by running a newspaper advertisement comparing its Temptations chocolate to the war-torn region of Kashmir. The ad carries the tagline: "I'm good. I'm tempting. I'm too good to share. What am I? Cadbury's Temptations or Kashmir?". To make sure nobody misses the point, the ad's creators laid the "too good to share" catchline over a map of Kashmir.

The ad has caused a national outcry. Indian politicians, shocked at the very mention of sharing the territory, threatened nationwide protests. It did not help that the ad was timed to appear on August 15th, India's Independence Day. And Cadbury's British roots have made the ad even harder to swallow. After all, it was British colonial rulers who, at par-

As companies try to get more staff to work on the road or from home, they lose the water-cooler conversations that sometimes spark useful ideas. Margaret Exley, chairman of Mercer Delta, a consultancy, argues that some employees, especially in customer services, rarely see their boss's face, even for a performance appraisal. Some sales teams get round this by having regular meetings on the road. One beneficiary of this trend is Starbucks, a coffee chain that is increasingly used as a substitute office. Several stores have even turned spare space into meetings rooms, according to Howard Behar, Starbucks' president for North America.

Companies with scattered staff also often try to bring them together in occasional conferences—and these have become much more intensive, carefully planned affairs. That partly reflects a shortage of corporate cash for jamborees. Ed Griffin, head of Meeting Professionals International, a trade association of meetings planners, says dolefully that finance executives have recently taken over responsibility for meetings budgets from sales and marketing departments. He worries that they may not grasp the extent to which a well-run conference can motivate sales staff. It is, he says, a matter of transmitting emotion, not just facts: "If you do it on a television screen, you lose 50-75% of the ability to create valuable relationships." If he is right, then companies will need to think even harder in future about how to make those eyeballs count. ■

tition in 1947, drew the boundary line between India and Pakistan that the two nations have battled over ever since.

Though Cadbury India has apologised, the timing is hardly good. Cadbury-Schweppes is in the process of buying the part of Cadbury India that it does not already own. And Cadbury is particularly sensitive about its image at the moment, since it is considering whether to jump into bidding auctions for Hershey Foods and Adams, two of the choicest confectionery companies to come up for sale in years.

While the gaffe might seem like a gift for the anti-corporate brigade, it actually shows that, even in peripheral markets, multinationals can't hide their blunders for long. And this week, WPP, a marketing giant, gave a warning that the worldwide advertising industry could remain in the doldrums for at least another year. A spot of subtlety might help.

Face value Fit for Fiat?

Gabriele Galateri hopes to rescue Fiat for the Agnelli family



NOBODY doubts Gabriele Galateri di Genola's intimate knowledge of Fiat, Italy's largest industrial group. After all, he has worked since 1977 for the Agnelli family, which founded Fiat over a century ago and still has a controlling interest with a 30.5% stake. During the 1980s, he rose to become group finance director, before moving across the Agnelli empire to run IFIL, an investment holding company through which the family sought to diversify away from car making. He has even been sitting on Fiat's board since 1996.

However, some observers reacted to Mr Galateri's appointment in June as chief executive of the troubled company by asking whether he has what it takes to turn things round. By any measure Fiat represents an enormous challenge. The group has a crushing net debt of €5.8 billion (\$5.6 billion) which it is struggling to reduce through a mixture of cost-cutting and disposals. Its car-making division, Fiat Auto, has been badly managed and looks set to lose more than €1 billion this year on top of heavy losses in recent years. Other divisions, such as Iveco (lorries) and Case New Holland (agricultural machines) are also in difficulty in today's weak markets.

This is neither the first time that Fiat has been in trouble, nor the first time that new management has been parachuted in to tackle a crisis. In 1980, for example, Cesare Romiti took charge when Fiat teetered on the brink of bankruptcy. An experienced industrial manager, Mr Romiti rescued the group by brutally restructuring its operations.

Mr Galateri's task is equally daunting. Unlike Mr Romiti, he has no hands-on experience of running an industrial concern. Rather, he boasts an impressive record as a financial manager. At IFIL, working closely with Umberto Agnelli, the younger brother of Gianni, the family patriarch, Mr Galateri increased the initial assets of €775m in 1988 into a portfolio

now worth around €3.8 billion.

More than half of IFIL's money is invested in service industries, including retailing and financial services, and less than one-sixth is now tied up in Fiat. Mr Galateri's successful strategy was to invest in non-cyclical industries that would offset the swings in profits that are typical of the car industry.

A personable man, he is intellectually curious and has a reputation as a good listener. His style at IFIL combined financial prudence with active involvement in the management of portfolio companies. An investment in SanpaoloIMM, Italy's second-biggest bank, where he sat on the executive board, gave him a thorough knowledge of the inner workings of commercial banks.

That should stand him in good stead in his new job at Fiat. The support of its commercial bankers will be vital in the coming months as Fiat tries to reduce its net debt to €3 billion by the end of this year. Paolo Fresco, Fiat's chairman, has publicly acknowledged that there is a fine line between a managed disposal of assets and the "fire sale" that could result from any new financial stumbles. Mr Fresco hand-picked Mr Galateri with the strong support of the Agnellis, presumably trusting in his ability to avoid further mishaps.

Mr Galateri has other important points in his favour. For Fiat, he represents a known and respected quantity, and the group's bankers see him as a credible interlocutor. Recognising that he needs to brush up on industrial know-how, he has already brought in a veteran plant manager to act as his adviser. With his strong record as a portfolio manager, he should quickly grasp whether Fiat's assets can be reshaped into something coherent and financially viable.

There is, however, a world of difference between building a portfolio from scratch and tackling an established set of businesses with deeply entrenched problems. Privately, senior Italian investment bankers wonder whether Mr Galateri is simply too close to the Agnelli family to be able to take the necessary harsh decisions. Despite this, the Agnellis seem genuinely to believe that he represents the best hope for rescuing Fiat.

In typically prudent fashion, Mr Galateri has asked for a few months to figure out a strategy, and has described his challenge as "long term". In practice, he will

have little time to present Fiat's banks with evidence that he is on top of the job. That will certainly include a clear plan to bring losses at Fiat Auto under control, seen by outsiders as a prerequisite for selling the business to General Motors in 2004, as allowed by a put-option agreement made when GM took a 20% stake in Fiat two years ago.

Mr Galateri may be forced to shrink the car business, in what would no doubt be seen as a repeat of the traumatic purge led by Mr Romiti two decades ago. Also to be tackled is Fiat's once visionary, but now struggling, emerging-markets strategy. Big manufacturing operations in Argentina, Brazil and Turkey have been bleeding cash, with no immediate prospects of improvement.

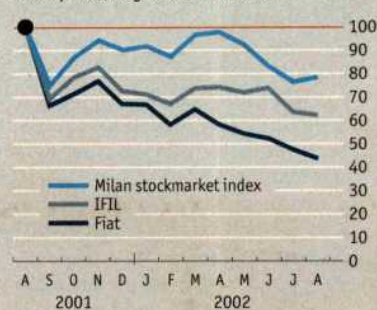
A bigger, better IFIL?

The enormity of the task raises the question of why, at the age of 55, Mr Galateri accepted it. At IFIL, he had a comfortable, even pleasant, position. Indeed, as recently as May he was answering speculation about an imminent move to Fiat by saying he was perfectly happy where he was, thank you. Now he has taken the biggest risk of his career. Was he pressured? Probably he was, but he is too loyal to admit it.

Imagine if he succeeds, however. In effect, he will have created a second IFIL, but on a much larger scale and with much more influence across European industry. Crucially, he will have helped the Agnellis finally to escape the troubled legacy of cars and metal-bashing. His reward would almost certainly be to succeed Mr Fresco as chairman. A pipe-dream? Perhaps, but a reason to accept an otherwise unpalatable position. ■

Trading down

Share prices, August 20th 2001=100



Source: Thomson Datastream



Cleaning up global banking

The repentant banker

The limits to removing banks' conflicts of interest

FIVE months ago accepted wisdom held that corporate and investment banking could achieve great economies of scale. Banks could get their foot in the door of a company by lending to it at generous rates, with the promise of profitable investment-banking business in the future. As proof that the strategy was paying off, the world's biggest full-service banks, Citigroup and J.P. Morgan Chase, were racing up the capital-markets league tables. The "pure" investment banks, such as Merrill Lynch, Morgan Stanley and Goldman Sachs, were under pressure to get out their cheque books and offer cut-price loans too—and so they did.

The collapse of Enron and WorldCom, and a general credit crunch, have changed the game. Lending has become more expensive, and rightly so, to reflect more closely the risks of companies defaulting. Meanwhile, investment banking is under powerful public scrutiny: exactly how do these guys, especially not-so-humble research analysts, justify such huge pay cheques? Last week Jack Grubman, once Wall Street's most celebrated telecoms analyst, resigned from Salomon Smith Barney, part of Citigroup, taking \$32m of severance pay with him.

New York state's district attorney, Eliot

Spitzer, is leading investigations into individual firms—an exercise that is fast turning into a cross-examination of the entire industry. Why stop at research analysts? CALPERS, the pension fund for California's public employees, joined the hunt this week: its board voted to withhold business from bond and equity managers who could not clearly demonstrate their freedom, and that of their analysts, from conflicts of interest. It could cut deeply into the way some financial firms do business.

Citigroup's chairman, Sandy Weill, rushed earlier this month to be the first on Wall Street to embrace Mr Spitzer's proposals. He has also promised that his firm will no longer sell complex financial products to companies that do not fully disclose the effect on their balance sheet (ie, no more special-purpose vehicles to hide the true nature of a firm's indebtedness).

For a moment there seems to be convergence between Wall Street firms, anxious to appear squeaky clean, and regulators and investors demanding more transparency. But how long before this unusual alliance brings tears? Seeking out conflicts of interest in investment banking is like peeling an onion. It could go on and on until there is little or nothing left. Take equity trading. It does not require much digging to

unearth potential conflicts of interest at firms with even the purest (that is, the simplest) business. Even that singular man, the so-called specialist on the New York Stock Exchange, trades both for himself and on behalf of clients.

In the wholesale markets for bonds, derivatives and other exotic products, few checks exist to ensure that prices are transparent and that privileged information is not abused. There is a question of perception: one person's synergy (the happy combination of abilities and information) is another person's conflict of interest (ruthless exploitation of privileged foreknowledge). What appeared to be synergy in a bull market, suddenly, in a bear market, looks more like conflict. If all this and more were drawn out into the daylight, precious little would be left of the fabulous returns investment banks and their staff are used to getting.

You'll be sorry

Yet there may be a reason, say investment bankers in their defence, why even the most militant of investors would be unwilling or unable to go so far. Bankers protest that unbundling or putting businesses and competencies into different compartments behind Chinese walls will not suit investors. Unbundling, they argue, is fundamentally uneconomic, and the investor will pay: in terms of the cost of fully independent research; and, still more, in a wider margin between selling and buying securities—because the traded market will be less liquid. Moreover, say investment bankers, most wholesale and investment-banking business is done among professionals able to look after themselves. ►►

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Proponents of the model of integrated banking are adamant that it has not been discredited by recent events. The subsidised lending was done largely to firms of good standing that were hardly expected at the time to be caught by a cyclical downturn. J.P. Morgan Chase was hit harder than was Citigroup by concentrated exposure to such firms, partly because it has merely half Citigroup's capital, and thus fewer chances for diversification. It is a blip that does not disqualify the model, these bankers insist. Big banks in general have survived remarkably well since the onset last year of a credit crunch, and have continued to make new loans to cash-strapped companies. Mr Weill said in the past that his bank should have the capital to survive all weathers, and so it has.

Yet a deep-seated problem in the sector must be the presence of too much capital chasing too high a return. Investment banks are still aiming at returns on equity of 20-25%. That might be more attainable if they had less capital, and indeed their falling share prices have done a good job of re-

ducing the problem. But there may, and probably should, be much more slimming to come.

New lessons have been learned in the past few months about diversification and the management of credit risk. Reputation risk (in particular, the risk of being tainted by your customer's lack of honesty), litigation risk and conflicts of interest have moved high up the agenda. Will this lead to a leaner, cleaner financial-services sector?

In fact, one of two outcomes is likely. Either investment bankers and analysts will be back to their old tricks within six months. Or increasing attention will be paid to greater transparency in the raising and allocation of capital. Under the second, more desirable outcome, financial intermediation will aim to be more of a service, less of an ego-trip for the participants, and considerably less well paid. But no one should expect too much. Mr Spitzer and the board of CalPERS have thrown down the challenge. Yet financial markets follow cycles—and that probably goes for the contrition of investment bankers. ■

right. But that target is possibly too low. The closer inflation is to zero, the harder it is to get the negative real interest rates often necessary in a recession, since nominal rates cannot go below zero. Research by the International Monetary Fund suggests that, if average inflation targets are set below 2%, then there is a marked increase in the risk that interest rates will hit zero and that deflation may occur. It might therefore be safer if the ECB aimed for a higher inflation target, with a mid-point (not a ceiling) of 2.5%. In which case, interest rates ought now to be lower.

Even assuming that rates are right for the euro area as a whole, policy looks uncomfortably tight for Germany. Its inflation rate is only 1%. And, thanks to weaker growth, the country's output gap (actual GDP less trend GDP) is estimated at minus 3%, twice as large as in the rest of the euro area. A way to gauge the appropriate level of interest rates in Germany is to consult the Taylor rule, devised by John Taylor, currently at America's Treasury Department. This calculates the "correct" interest rate according to the inflation rate and the size of the output gap. It suggests that the German interest rate should now be a full percentage point lower than that set for the euro area as a whole.

In theory, if a country cannot cut interest rates, because of monetary union, it should use fiscal policy to support its economy. Yet Europe's stability and growth pact does not allow euro-area governments to borrow more than 3% of GDP (see page 56). On current policies, Germany's budget deficit may breach 3% of GDP this year. Under the stability pact's rules, that would force the government to tighten policy, further depressing its economy.

From America with love

A popular excuse for euro-area weakness, including Germany's, is that exporters have been hurt by America's downturn. Yet net exports from the euro area have increased over the past year. It has been weak domestic demand, not external demand, that has dragged down economies. In Germany, exports have been the only

European economies

Double-dip in Germany?

The ECB's monetary policy is much too tight for Germany

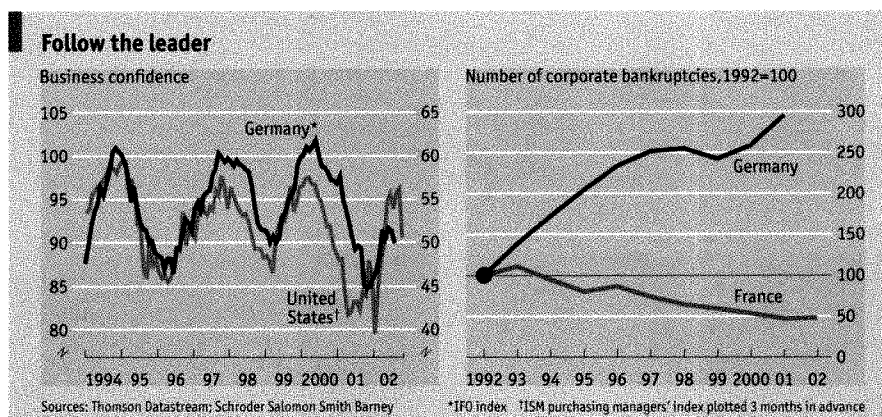
WHY are the euro-area economies so weak, and Germany's in particular? Before the euro was launched, German policymakers fretted that the European Central Bank (ECB), influenced by countries with high jobless rates, such as France and Italy, would pursue a laxer monetary policy than would the old Bundesbank, and so hold interest rates too low. The opposite has happened. Interest rates are currently higher than if monetary policy had been set according to conditions in Germany alone. As a result, Germany's economy has been squeezed.

Germany's GDP grew at an annual rate of only 1.1% in the second quarter of this year, leaving it just 0.1% higher than a year ago. Italy's economy also grew by a paltry 0.9% in the second quarter, but the other two big economies, France and Spain, are expected to show stronger growth. Even so, a recent slide in business confidence has caused many economists to trim their forecast for growth in the euro area in 2002, to around 1%. Germany will be lucky to achieve half that. By contrast, the United States is still tipped to grow by over 2%.

So why does the ECB not cut its interest rate, currently at 3.25%, compared with America's rate of 1.75%? The ECB still frets about inflation. The headline rate for the

whole euro area, at 1.9%, is a whisker below the 2% ceiling of the ECB's target, but core inflation, excluding food and energy, is 2.5%. Most economists do not expect rates to be cut this year. This raises two questions. First, are rates currently appropriate for the euro area as a whole? Second, how much lower would they be if the Bundesbank was still setting interest rates to suit Germany alone?

Given the ECB's inflation target of "below 2%", which can be interpreted as a range of 0-2%, most economists reckon that interest rates in the euro area are about



► source of growth: consumer spending and investment have fallen over the past year.

Even if weak export markets cannot be blamed, the bursting of America's economic bubble has squeezed spending in other ways—through foreign investment, share prices and business confidence. Following a wave of acquisitions in the 1990s, European firms' dollar sales from their American subsidiaries are now four times bigger than their exports to America. America's slump has therefore squeezed parent firms' profits in Europe, forcing them to cut investment back home.

European share prices have also tracked Wall Street more closely than usual—or have fallen further. German equities have fallen by 52% from their peak in 2000. This is more than in other European markets and more than the 40% fall in America's S&P 500 index. Only one-fifth of Germans own shares, compared with half of Americans, so the direct wealth effect is smaller. The indirect effect, through confidence, could be disproportionately large.

In recent years the correlation between indicators of business confidence in America and in the euro area has increased. The mood of European businessmen seems to follow the mood swings of American bosses a few months later. The correlation is closest for Germany (see left-hand chart on previous page), where businesses are most exposed to the American market, after buying lots of companies there.

Do European economies have financial imbalances akin to America's? Household saving rates are much higher and the euro area has a current-account surplus, in contrast to America's big deficit. However, Europe is far from being a model of financial prudence. The total debts of non-financial companies in the euro area have climbed, from 47% of GDP in 1997 to 58% at the end of 2001. The debts of American companies also rose sharply, yet are still lower, at under 50% of GDP. Total household debt as a share of GDP is also higher in Germany than in the United States. Slow growth, very low inflation and high debts are a painful combination.

Michael Saunders, an economist at Schroder Salomon Smith Barney, reckons that corporate balance sheets are more fragile than generally assumed, especially in Germany. Corporate bankruptcies in Germany are running at three times their level in the early 1990s; in France they are half their level of a decade ago (see right-hand chart on previous page).

Many German companies, in other words, look as stretched as do their American counterparts. But, unlike companies in America, German ones have no monetary guardian to rescue them by cutting interest rates. The risk of a double-dip recession, and perhaps even of deflation, might therefore be higher in Germany than it is in the United States. ■

Deposit insurance in Japan

Rug not pulled yet

TOKYO

Another fudge?

COMING up with fresh ways to fudge deposit-insurance reform is a hobby of Japanese politicians. A previous two-year postponement, supposed to give the government extra time to clean up the banks, left them weaker than before. Now the government is thinking of breaking its promise to lift its guarantee next April on ordinary deposits of over ¥10m (\$84,000). On August 19th, Standard & Poor's (S&P), a credit-rating agency, argued that such a setback to reform could send Japan's rating even lower. Weak banks, says Naoko Nemoto of S&P, would stumble on, frustrating a banking recovery.

Not, of course, that the government is officially considering any postponement at all. Banks, it says, are healthy, and reform will go ahead as planned—except, that is, for one small change.

The change, which a special panel is considering at the request of the prime minister, Junichiro Koizumi, would keep fully protected the current accounts used by big firms and local governments for settlement purposes. So that individuals do not feel left out, new accounts for small depositors would be allowed that also receive blanket protection, but yield no interest. That would be tantamount to halting deposit-insurance reform, critics say.

Getting the scheme to work will be hard, not least because most banks oppose it. Creating new types of account takes time, and is costly. Bankers doubt the accounts could be ready by next April.

The government and banks are also

split over who will pay the extra deposit-insurance premiums. Banks are reluctant. Since these settlement accounts offer no interest at all, banks cannot pass the costs on to depositors, in the form of lower interest rates. So they will have to ask for high account-management fees. Banks, especially the weak ones, wonder how many depositors would be willing, in effect, to pay banks to use their money. Banks want taxpayers to foot the bill instead, to which the government is unlikely to agree.

If the aim is to prevent a rash of bank failures—by discouraging depositors from moving their money away from weak banks into safer ones—then it will not work anyway, Brian Waterhouse of HSBC Securities argues. Look no further than Hokkaido Takushoku Bank, which failed in 1997, he says. Although its deposits were fully protected by the government, depositors still fled to bigger banks, or to the postal savings system. This latest scheme is worse, because it will have to require all the banks to act simultaneously. If they did not, then banks offering the special guaranteed accounts would immediately be seen to be desperate—perhaps leading to the runs on deposits that the scheme seeks to avoid in the first place.

With so many drawbacks to his latest suggestion, Mr Koizumi may wonder whether it is worth damaging his reformist credentials even further. Another idea is to extend protection of ordinary deposits, on the condition that banks lower the interest rates on these to zero (from about 0.001% currently), has similar pitfalls. Still, the fudge helps lessen pressure from the old guard in the Liberal Democratic Party. Mr Waterhouse thinks that the prime minister might use the banks' argument that they are having trouble getting their computer systems ready in time as an excuse to keep the safety net in place for another year—all the while insisting that the reforms are still on track. ■



So you see, your money's safe with us, sir

World Development Report

Sustaining hope

Is the World Bank turning Marxist?

STRANGE goings-on at the World Bank. Not long ago, its director for the environment, Kristalina Georgieva, asked her team a question: why care about nature? Given the bank's focus on poverty, she said, the reason was surely its impact on human welfare. After all, as the bank itself has noted, environmental problems such as air and water pollution are the leading preventable cause of health ailments in poor countries. Yet when she made that point, half the audience disagreed. One green staffer even left the room in a huff.

Now comes another apparent sign of heterodoxy. On August 21st the agency published its annual World Development Report (WDR). The theme and timing of this year's report coincide with the United Nations summit on sustainable development, which starts in South Africa on Au-

gust 26th. If the World Bank seemed a shade green before, a casual reader might think it has now turned positively red.

For a start, the report suggests that economic growth, long seen by liberal economists as the surest route to poverty alleviation and environmental improvement, is not enough. It explains that sustainable development is "about enhancing human well-being through time", which means helping people to improve such things as their "sense of self-worth" and not just their net worth.

The WDR also rejects the view that despoiling nature is an unavoidable yet reversible companion to economic growth. Environmental problems are, "at their root, social problems. The distribution of assets, and of the costs and benefits of different policies, as well as the role of trust, are all critical to the ability of societies to develop competent rules and institutions to address environmental, social and economic problems." The report argues that the "poor and disempowered" must have much greater access to assets if growth is to be sustainable and the world is to avoid social unrest.

So does the WDR really add up to a neo-Marxist call for the redistribution of as-



A preventable cause

sets? Not at all, insists Zmarak Shalizi, its lead author: "Our arguments are grounded in neoclassical economics and game theory." He notes that his team defines a society's assets as including far more than merely land, labour and capital. Property rights, the rule of law, transparency and even trust count, too.

Besides, Mr Shalizi argues, these assets are already being "appropriated" in many societies by powerful individuals, governments, firms or bureaucrats. That explains why otherwise sensible policies—including ending environmentally damaging subsidies—are often thwarted. "The benefits of such policies are often dispersed, but the costs concentrated, so the policies get captured by a few." Strong institutions must compensate for this, he insists.

The bank argues that its emphasis on asset allocation need not provoke a backlash from fat cats: future economic growth will create plenty of new assets to spread around. Over the next five decades, the authors reckon, world output could quadruple, to \$140 trillion, and the world's population rise to 9 billion, with humans a chiefly urban species for the first time in history. To most of those heading for the summit, this will sound like a nightmare. Yet, while acknowledging the pressure this will put on the planet, the WDR authors insist these trends could be good news too.

For a start, they note that the real news on population is that its growth rate is moderating. As a result, the coming years will see a boom in people of working age. Mr Shalizi adds that economic growth deriving from this will create an enormous stock of new assets that can be shared with the world's poorest. Even the migration to cities can be positive, for it means the poor can share in the new jobs, educational opportunities and housing stock to come.

All this, the WDR reckons, adds up to an opportunity to make growth more inclusive and sustainable. That is a surprisingly hopeful stance, given that sustainability gurus are usually a gloomy bunch. The summiteers in Johannesburg could do worse than to read this report. ■

South African fraud

Scam of scams

JOHANNESBURG

How to impersonate a central bank

IF YOU must tell lies, tell very big ones. Last week a gang in Johannesburg were caught telling a whopper: they were masquerading as South Africa's central bank. African con-artists, mostly from Nigeria, have long run a racket known as the "419" scam, or advance-fee fraud. Gullible types overseas are persuaded that great piles of cash stolen by an African general, warlord or minister are mysteriously available. The victims are asked to store the money in their bank account, in return for a share of the loot. But first they must pay a few thousand dollars—to cover expenses, you understand. Each year, amazingly, thousands of credulous victims pay out, with never a cent in return.

Such scams have become two-a-penny, partly because red-faced victims rarely come clean to the authorities. But as Nigerians earn a reputation for dodgy deals (the 419 racket is named after the number of the Nigerian law that forbids it) con-men are moving to southern Africa. One group recently sought partners to "share" in millions of dollars of the late Jonas Savimbi, the Angolan rebel leader.

The latest swindlers set up a website

purporting to be that of the South African Reserve Bank. They e-mailed folk in Britain and America to say that money could be siphoned from the bank to their own accounts. Doubters could double-check names, photos and mobile-phone numbers online, and visit an accompanying (and also fake) website of a law firm to draw up legal documents. Of course, the victims were also told to send "facilitation payments" to anonymous bank accounts, and to keep quiet about the deal. Many people are reckoned to have sent money. One Briton alone, says Sipho Ngwema, of the police investigating team, was defrauded of 2m rand (about \$200,000).

South Africa worries that such scams will sully the country's name. The finance minister, Trevor Manuel, wants a call-centre set up by September, so that investors can check on local businesses without relying on websites. That should help against pyramid schemes and fly-by-night operators, but it will not guard against scams that depend upon victims' complicit silence. Next time that Savimbi's daughter or Mobutu's cousin e-mails you with a promise of riches, press delete.



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Economics focus The case for co-operating

Europe's stability and growth pact is producing perverse results

AS THE River Elbe burst its banks this month, the German government's budget deficit threatened to breach the limits of the euro area's "stability and growth pact". The pact prohibits fiscal deficits above 3% of GDP. Except in severe recessions, they can attract a fine of up to 0.5% of GDP. Germany now has a deficit of 2.8%. This week, Gerhard Schröder, Germany's chancellor, delayed popular tax cuts in order to be able to dispense flood aid without violating the pact. With an election coming up, this is a political embarrassment. Portugal, which admits to a fiscal deficit in 2001 of over 4%, already faces the prospect of punishment. Conceivably, France and Italy may also test the limits of the pact before long.

A decade ago, the pact's architects, most of them German, feared that the euro's credibility might be undermined by fiscal laxity among its members. If a government's borrowing becomes unsustainable, its central bank might be forced to bail it out, inflating away the real value of its debts. Such bail-outs are expressly forbidden in the euro area, while the European Central Bank (ECB) enjoys a forbiddingly strong position relative to national-level fiscal authorities.

Prudent or not, the euro area's 12 finance ministers remain accountable for their fiscal choices. If they court insolvency, financial markets will apply a risk premium to the government's bonds, or refuse to lend to them altogether. Why should the European Commission try to police sovereign borrowing when the markets already do so? If anything, monetary union calls for granting more fiscal discretion to national governments, not less. Having ceded monetary policy

to the centre, member nations have greater need of fiscal flexibility to cope with problems that afflict them at home.

Germany is a case in point. If it were still in a position to conduct its own monetary policy, interest rates would now almost certainly be lower. Meanwhile, a weak German economy probably needs precisely the kind of tax cuts that Mr Schröder was forced to shelve this week. In other words, the pact's "excessive deficit procedure" looms large at precisely the moment it will do most harm. Germany may yet escape fines, by invoking a special exemption for events beyond its control—observing the letter, if not the spirit of the pact.

The pain of solitary punishment

The pact may be flawed, but the euro area still has fiscal problems which its members need to address. Between 1990 and 1996, the future euro-area members ran an average deficit of well over 4% of GDP. Stronger economic growth, along with the tough rules of the stability pact, have since forced that figure down, to 1.5% on average. But now that "Maastricht fatigue" may be setting in, those deficits may widen again. Euro-area government debt stands at 72% of GDP, a deal higher than the 60% figure the Maastricht treaty deemed sustainable. Many European governments face hefty pension liabilities in the near future. If Europeans are serious about putting their budgets in order, they will need to undertake long-term fiscal reforms. Is it better that they do so singly, as and when the pact forces them to, or together, as part of a collective effort?

Christopher Allsopp and David Vines of Oxford University, together with War-

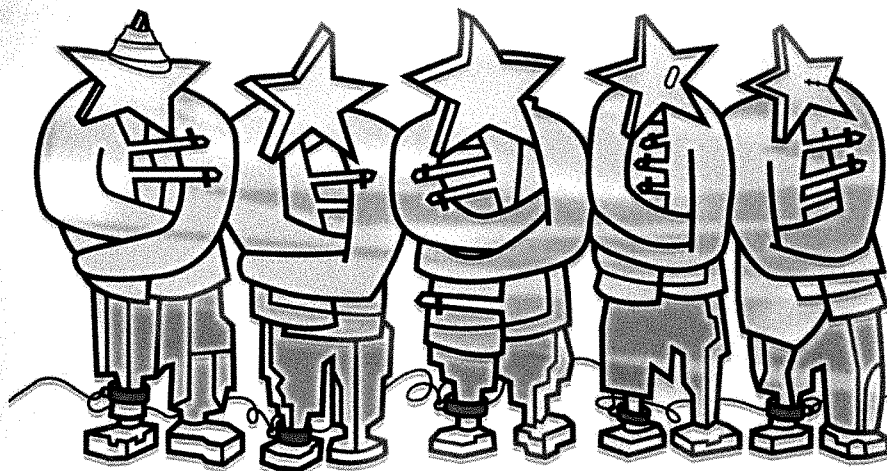
wick McKibbin of the Australian National University, argue against going it alone. Budget cuts are never painless, but within a monetary union individual cuts can be excruciating. A country with an autonomous monetary policy can offset tighter fiscal policy by expanding credit and devaluing the exchange rate. But in a monetary union, where an individual country can no longer cut interest rates, nothing cushions the blow.

The authors asked what would happen if France were to cut its budget deficit unilaterally, by 2% of GDP. According to their simulation, French output would fall by more than 2%. Prices would fall a bit in France, but across the euro area as a whole they would barely change. So the ECB would have little cause to cut nominal interest rates. As a result, the real rate of interest—nominal rates adjusted for inflation—would actually rise in France. Output would eventually recover, but not before a recession of up to three years.

What if France agreed with the other member states to cut deficits together? Surely, a synchronised contraction would be even more damaging, as each country's recession spilled over into its neighbours' economies. Possibly, the authors acknowledge. Yet, while the ECB might not respond to a slowdown in one country, fiscal austerity in all 12 euro countries would probably force it to cut rates, so bolstering private spending even as government spending falls. A rate cut would also weaken the euro, boosting exports.

Investors might provide another cushion. Collectively, the euro area accounts for a big share of the demand for global savings. As they reduced their claims on these savings, Europe's governments would take pressure off the world's long-term real interest rates, boosting share prices and "crowding in" private-sector investment.

If fiscal reforms are undertaken jointly, the short-term sacrifices may be surprisingly light, and the long-term benefits may arrive surprisingly early. Such a happy outcome hangs upon pursuing reforms that are both credible and co-operative. It is a pity, then, that Europe's stability and growth pact, as it stands, is neither. ■



* "Fiscal Consolidation in Europe", by Christopher Allsopp, Warwick McKibbin and David Vines, in "Fiscal Aspects of European Monetary Integration", Cambridge University Press, 1999.



Biotechnology in Singapore

Send in the clones

SINGAPORE

Will a relaxed attitude to regulation make Singapore the stem-cell-research capital of the world?

A YEAR ago, when George Bush was ruling on the future of human stem-cell research in America, no Singaporean university even taught advanced cellular biology. There was only one prominent researcher studying stem cells in the whole of the country—and his work was going to waste. Ariff Bongso, the scientist in question, was the first to isolate human stem cells (whose function is to turn into other types of cell and which may thus, some hope, be used to regenerate damaged organs, or even to clone existing individuals). He did so in 1994. But Dr Bongso did not patent his technique, allowing American colleagues to steal a march on him.

Now, the boot may be on the other foot. In August 2001, Mr Bush placed restrictions on federal-government funding for research into human stem cells because of ethical concerns about cloning and abortion (aborted fetuses are a good source of stem cells). Moreover, Congress is debating legislation that would further restrict stem-cell research, regardless of where the money comes from. The pace of research in America has slowed markedly as a result—and the government of Singapore has seen an opportunity. By turning itself into a “regulatory haven” for stem-cell research, it hopes to attract disaffected scientists who feel their freedom to investigate is compromised elsewhere.

Giving safe haven to stem-cell research is part of a wider government policy. In 1999, life sciences, ie medicine, pharmaceuticals and biotechnology, were designated one of the country’s four “industrial pillars”. The idea was to build a “knowledge economy” which would continue to generate growth long after traditional industries such as petrochemicals and electronics had fled to cheaper places. The only hitch was that Singapore had few companies, research facilities or personnel with any experience in the field.

But what Singapore’s rulers want, they usually get. Within the space of two years, they have set up two new university faculties and five new research centres, and funnelled S\$3 billion (\$1.7 billion) into a series of funds designed to promote research, attract international life-sciences firms and finance local biotechnology businesses. The first phase of one-north, an industrial-cum-research-cum-theme park (itself a novel combination of ideas) that will cost S\$15 billion, will open next year. The timetable for bringing all this into being was so tight, according to James Tam, an American academic recruited as dean of one of the new university faculties, that he had to start interviewing potential professors the day he arrived in Singapore, having read their applications on the plane over.

Recruiting big names has been an im-

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portant part of Singapore’s efforts to lend credibility to its biological ambitions. Alan Colman, the head of the team of researchers that cloned Dolly the sheep in Scotland, has just joined esi, an Australian firm lured to Singapore by government funding. Edison Liu, until recently a leading researcher at America’s National Cancer Institute, is now the head of Singapore’s new Genome Institute. Yoshiaki Ito was poached, complete with his research team, from Kyoto University, to join the Institute of Molecular and Cell Biology.

Gene sling

The main draw for such luminaries, apart from the rock-star status accorded them by the local press, is Singapore’s permissive climate for research. For example, the government actively encourages work on stem cells rather than grudgingly permitting it. It also allows cloned embryos to be kept for up to 14 days. No country goes further than that. Just as important, it takes little time, paperwork or glad-handing to get approval—and generous funding—for research proposals, according to Dr Tam.

How quickly—if at all—such licence and largesse will turn into products remains to be seen. Dr Colman is planning to work on inducing stem cells to turn into insulin-producing “islet” cells, which could be implanted into diabetics. Some of his colleagues at esi want to turn them into nerve cells to replace those lost in Parkinson’s disease. These are plausible ideas, but will take years to come to fruition.

A possible straw in the wind is that earlier this month, Dr Bongso managed to solve a problem that could have bedevilled future stem-cell therapies. At the moment colonies of human stem cells have to be grown on layers of tissue derived from

rice. This technique carries the risk that viruses present in the so-called "feeder cells" might jump into the stem cells. That would prevent such cells being used therapeutically, because they might carry the infection to the patient. Dr Bongso, however, has managed to derive feeder cells from human tissue, and this time, he has been sure to patent his invention.

But turning that patent into applied medicine—and profits—will require the input of investors and managers as well as researchers. Furthermore, Singapore is not known as a febrile crucible of ideas and innovation. It can import academic grantees, just as it has foreign firms, but that might not prove enough to spark the creative "buzz" of a successful economic cluster. The government's efforts to generate such an atmosphere by decree only serve to underline how paternalistic it remains. One of its many glossy pamphlets, for example, gushes about a "live-work-play environment that will create a unique DoBe lifestyle" (whatever that may be). It depicts young, good-looking, racially diverse scientists playing trombones, sipping fruity cocktails and walking barefoot in the park. But, as the same brochure cryptically points out, "Innovation does not occur where it is supposed to." ■

Tropical agriculture

Trees of life

BERKELEY, CALIFORNIA

A new twist on an old idea is improving farm yields in Africa

SOUTHERN AFRICA is currently facing its worst food crisis for more than a decade. Around \$500m-worth of aid is thought to be needed to feed the millions at risk of starvation. In that part of the world, and in Africa more widely, a large obstacle to food production is the poor agricultural yield that results from over-use of the land. With manure in short supply in many places—and artificial fertilisers beyond the means of most—it is impossible for nutrient-drained soils to be replenished with nitrogen. This helps to explain why Africa south of the Sahara is the only region of the world where food production per head has remained stagnant over the past 40 years.

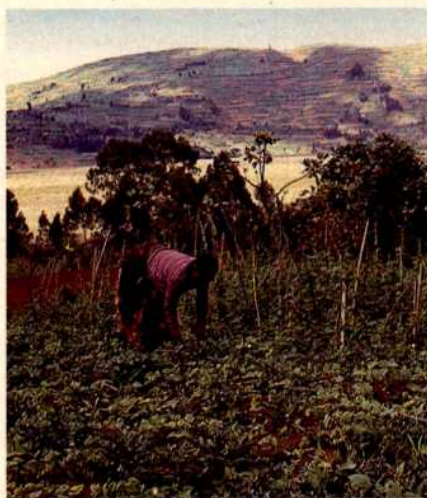
Earlier this month, Pedro Sanchez, head of the International Centre for Research in Agroforestry (ICRAF) in Nairobi (and also a visiting professor at the University of California, Berkeley) was awarded the World Food prize for his research into low-technology methods for improving soil fertility. The key to restoring fertility is to sow legumes. The roots of these plants

harbour bacteria that are able to extract nitrogen from the air and turn it into soluble molecules. Legumes use these molecules to make proteins. Plough the legume back into the soil and the nitrogen becomes available to the next crop.

Crop rotation using herbaceous legumes such as clover and alfalfa is standard practice in many parts of the world. Dr Sanchez's insight was to realise the advantages of planting leguminous trees instead. Herbaceous legumes have to be grown alternately with the primary crop. Trees, by contrast, can be planted at the same time, and have their effect before the following growing season.

This is how it works. At the beginning of the rains, both food crops and leguminous trees are planted. Because the trees initially grow slowly, there is little competition between them and the crops. In the dry season, though, after the crop has been harvested, the trees shoot upwards and reach three metres in height in eight months. During this time, trees drop their leaves, providing nitrogen-rich mulch, and they are then cut and harvested for poles or firewood. When the next food crop is planted, it benefits from the nutrients and improved physical properties of the soil that the trees have provided.

Dr Sanchez and his colleagues at the ICRAF tested 15 different species of leguminous tree, and found that the best of them will add between 100kg and 200kg of nitrogen per hectare during the course of a year—about the quantity that maize farmers add as artificial fertiliser. Using this system, crop yields go up dramatically, from one tonne to four tonnes of maize per hectare in a good year, and from zero to a tonne in a drought. A further, and unexpected, benefit of the system is in weed control. Crops are often damaged by witchweed, a widespread crop parasite that usually germinates after a cereal crop is planted. However, secretions from the trees' roots stimulate the germination of



Out of the woods

the witchweed seeds before crop planting. With nothing to feed on, the witchweed then dies, leaving the field clear for the next sowing season.

Convincing farmers to adopt new methods is always a challenge, but between 50,000 and 100,000 people in eastern and southern Africa are thought to be using the technique already. This is a good start, but it is only a fraction of the millions who might benefit. To reach those millions, says Dr Sanchez, would cost \$100m over the next decade. That would be excellent value for money—and certainly better than food aid. ■

Computer interfaces

No-touch typing

It is now easy to type by eye

HOW many fingers does it take to type? Ten, for the secretary trained to do it by touch. The keyboard clatters. Two, for the executive who never quite got to grips with computers. Tap, pause, tap. None, for anyone using Dasher. Look, no hands!

Dasher is a text-input program that works by predicting which letter is most likely to come next in a piece of text (and also the second most likely, third most likely etcetera). It then presents the possibilities to the typist on a screen. The typist chooses one, which is added to the growing text, and the program presents another set of choices. And so on.

Dasher's most recent incarnation, reported in this week's *Nature* by the program's originators, David MacKay and David Ward of Cambridge University, can literally be controlled by eye. A camera mounted next to the computer screen measures light reflected from the eyes. It works out which direction they are pointing and therefore which letter they are looking at, and transmits this information to the computer. After an hour's practice, typists can achieve a respectable 25 words a minute. So people such as quadriplegics, who have control only over their eye-movements, can communicate quickly and comfortably with a computer.

Dr MacKay and Dr Ward are not the first to try to replace the conventional keyboard, but they are perhaps the first to find a solution that is so much fun to use. The letters line up on the right-hand side of the screen in alphabetical order, top to bottom. Move the cursor towards them and they start to stream forwards, jostling and crowding. A letter is selected by steering the cursor into the coloured box that contains it. Within that box another set of let- ➤

ters then appears. The cursor moves ever deeper into the nesting boxes as letters are strung together. Not every letter is equal, however. Some loom large and appear at the centre of the screen while their neighbours are squeezed into tiny spaces.

This happens in response to a mathematical model that looks at the previous five characters in order to predict what might come next. Then it makes the most probable letters bigger so that they are easier to get to. The model knows nothing about English and does not even understand the concept of words. Instead, it uses statistical information gleaned from a training text (Dr MacKay used Jane Austen's "Emma"), to which it adds each time the program is run.

Dasher could make a significant difference to the small group of disabled people who can neither move nor talk. However, a much larger group, including everyone who owns a mobile phone, pocket computer or other gadget too tiny to accommodate a keyboard, might find it makes life more convenient. The program could be put into these devices and operated with a mouse, tracker-ball or stylus, instead of an eyeball. Dasher could also compete with the speech-recognition packages used instead of keyboards by those with repetitive-strain injuries.

Because it learns as it goes, the program can adapt to the vocabulary and style of its owner. Dr MacKay suggests that different versions could be marketed. "Yoof culture" for mobile phones perhaps, and "pompous novel" for the aspiring author. The software can be downloaded free at www.inference.phy.cam.ac.uk/dasher. ■

Preventing malaria

Another jab

A new malaria vaccine is being tested in the Gambia

MALARIA affects more than 500m people a year, and kills 2.7m of them. Three-quarters of those fatalities are children under five. Over the past 35 years, the disease is thought to have cost Africa alone \$100 billion in lost GDP. Yet, while powerful anti-malarial drugs and anti-mosquito compounds exist, a vaccine remains elusive. With luck, that will soon change. For this month a radical new design of malaria vaccine started its field trials.

All existing vaccines, for all diseases that can be vaccinated against, work by stimulating the production of antibodies (protein molecules that recognise, lock on to and disable invading viruses, bacteria and other parasites). Antibodies are an important arm of the immune system, but are not the only one. Another arm works by recognising and destroying infected cells, and it is this that Adrian Hill and his colleagues at Oxford University hope to encourage with their vaccine.

The malaria parasite has a complex life-cycle. After someone is bitten by an infected mosquito, the parasites first infect his liver. After a week, they break out of the liver cells that they have been breeding in and enter the bloodstream. Finally, they develop into a form that can infect other



Now with added CTLs

mosquitoes that bite the victim, thus restarting the whole process.

Vaccines that stimulate antibody production have proved ineffective against malaria. The stimulated antibodies are unable to deal with the parasites when they encounter them in the bloodstream, because at this stage of their life-cycle malarial parasites express a confusing array of different genes. To overcome the confusion, Dr Hill's vaccine is designed to provoke attacks on parasites when they are in the liver. Instead of stimulating the production of antibodies, it stimulates cytotoxic (ie, cell-killing) lymphocytes, or CTLs.

The active part of the vaccine is DNA cloned from the parasite. Two shots are needed. The first consists of "naked" DNA, and the second of a harmless virus that has had the cloned DNA added. The result, in both cases, is that the cloned DNA is translated into fragments of parasite protein that the CTLs can learn to recognise. Then, when such primed CTLs come across infected liver cells (which have the same fragments on their surfaces) they recognise the infection and kill the cell.

The new vaccine has undergone preliminary trials on 70 volunteers in Oxford. These tests showed partial but significant efficacy against a "high-dose challenge", which involved giving participants five bites from heavily infected mosquitoes. That is not ideal, but it is better than nothing. Also, the CTLs that resulted from the vaccine hung around (and presumably provided protection) for more than a year. The vaccine has not, however, previously been deployed in a malarial area.

The tests now starting, which are being carried out in the Gambia, involve 360 adults. Half will be given the new vaccine and the other half a rabies shot (which has the virtue of providing useful protection against a disease endemic in the area, rather than being a mere placebo). The subjects' health will be monitored during October, November and December, the country's malaria season. If the results are positive, the team hopes for a usable vaccine within a decade. ■

The CONTOUR mission

A bad break

Another spacecraft seems to have gone AWOL

HOPES are fading fast for NASA's cometary exploration mission, CONTOUR. The spacecraft, which cost America's space agency (or, rather, the American taxpayer) \$159m, was launched on July 3rd. Unfortunately, since an engine "burn" on August 15th, which was intended to launch it out of earth orbit and on its way, CONTOUR has been silent.

Comets interest astronomers because they are unaltered leftovers from the formation of the solar system, and may thus provide evidence that distinguishes between the various theories of that system's origin. CONTOUR was designed to carry out the closest flypast of a comet so far, and also to perform chemical analyses of at least two very different types of comet.

The silence is ominous, although past spacecraft have sometimes shut up unexpectedly, and then resumed contact. More worrying is that, since August 16th, telescopes have shown two objects travelling in the spot where CONTOUR ought to be. This has led to speculation that the craft broke up when its rocket motor was fired.

If CONTOUR receives no commands for 96 hours it is programmed to contact earth by itself. If that does not happen, the Applied Physics Laboratory at Johns Hopkins University, in Maryland, which is managing the mission for NASA, has said that a final effort to get in touch will be made in December when the craft's antennae will (if it has taken the path it was supposed to) be in a more favourable orientation.

Danish Ministry of Foreign Affairs Danida

Invitation to pre-qualification

Procurement Agents

As part of its efforts to reducing poverty through the promotion of economic growth with poor population groups as active participants, equal participation of men and women, popular participation in the development process as well as the strengthening of the rule of law and good governance Danida is planning to integrate procurement agents in the procurement of goods under its bilateral grant assistance.

Scope of Work

On behalf of Danida the procurement agent will buy local as well as imported goods required in connection with Danida's bilateral grant assistance to its programme countries being Bangladesh, Benin, Bhutan, Bolivia, Burkina Faso, Egypt, Ghana, Kenya, Mozambique, Nepal, Nicaragua, Tanzania, Uganda, Vietnam and Zambia.

The total annual Danida grant budget for its programme countries is approximately 3.8 billion DKK of which a minor part is used for the procurement of goods.

Danida will tender a Programme Country Enabling Agreement (PCEA) for each programme country. Based upon the PCEA the procurement agent will negotiate procurement agreements with the local Danish Embassy and when feasible also with Danida supported projects and sector programmes.

The remuneration of the procurement agent will partly be a management fee and partly transactional fees. It is envisaged that the PCEA will be for two years commencing late 2002. There will be possibility for a negotiated extension of the PCEA of up to further three years subject to satisfactory performance in the first two years.

Qualifications

The prospective procurement agent should demonstrate the following competences and capacities:

- Recent experience with assignments of similar nature and complexity
- Access to experienced and highly qualified local, expatriate as well as headquarter based procurement staff
- Financial viability
- Reputation for efficient and transparent execution of procurement agreements
- Knowledge of the Danish business sector

Pre-qualification will be limited to qualified firms or joint ventures which are legally incorporated in, and have their principal place of business in one of the member countries of the European Union.

Submission of pre-qualification documents

Further information as well as application forms are available at www.um.dk/danida/erhvervsliv/kontraktsekretariatet/pkval.asp

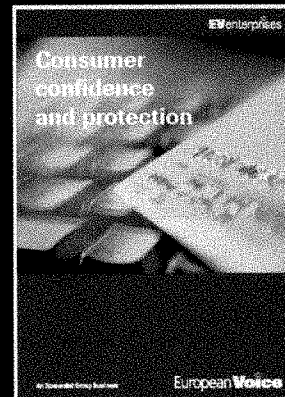
Applications for pre-qualification should reach the Ministry of Foreign Affairs, Asiatisk Plads 2, DK-1448 Copenhagen K, attn Mogens Strunge Larsen or by e-mail to pq@um.dk no later than 13 September 2002.

EVenterprises

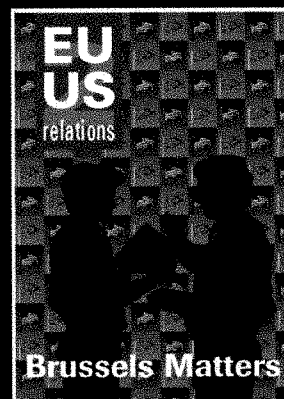
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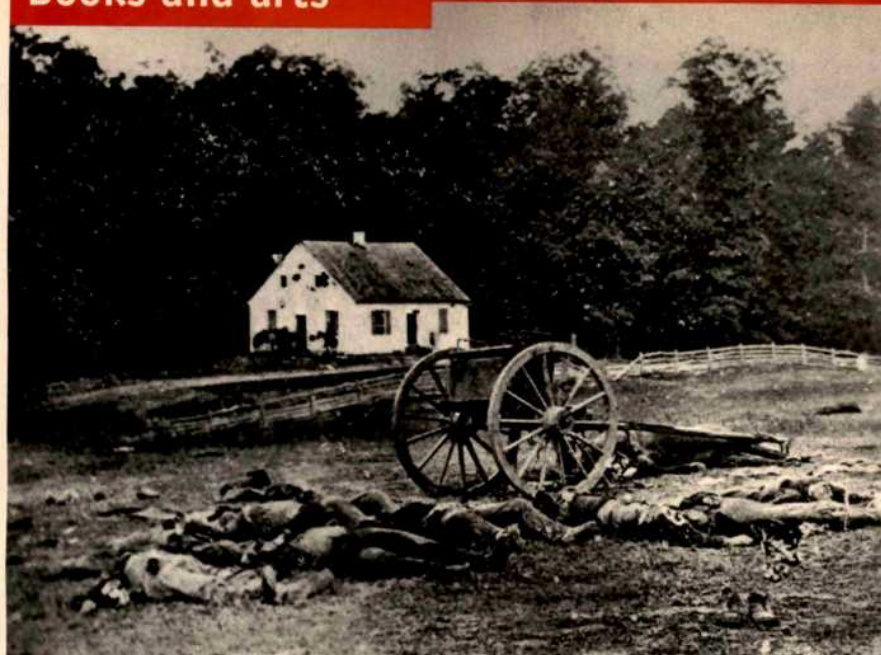
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American civil war

It led to total war

A master American historian reflects on the contingencies and unforeseen consequences of a single terrible battle

IT IS a great counterfactual question about the battle of Antietam, where more than 6,000 Americans died on September 17th 1862, the bloodiest single day in American history. The battle was a turning point when the war between North and South could have gone another way. What might have happened if the balance that day had been reversed and George McClellan's union army—not Robert E. Lee's confederate troops—had been the ones too scattered to fight?

James McPherson, a historian at Princeton and one of the leading authorities on the American civil war, is in no doubt of the answer. On learning of his opponent's disadvantage, the southern commander would have had his swiftest soldiers, Stonewall Jackson's "foot cavalry", on the march within the hour, with the dependable James Longstreet not far behind.

As it was, the over-cautious McClellan procrastinated although he had almost twice as many men as his foe. Through an astonishing series of lucky accidents, a verifiable copy of Lee's campaign orders had come into his hands. These revealed that his adversary had split his much smaller army into four widely separated parts. McClellan nevertheless took 18 hours to begin moving his men—all the time the nimble Lee needed to gather his forces to avert disaster. His army was mauled but left the field in good order, en-

Crossroads of Freedom: Antietam, The Battle that Changed the Course of the Civil War. By James M. McPherson. Oxford University Press; 203 pages; \$26 and £17.99

abling the South to carry on its fight for independence—as it turned out for almost three years. Had McClellan struck, as a bolder general might have done, the war could have ended then and there.

Though alive to these contingencies, Mr McPherson is less interested in virtual history than in consequences. He shows that the battlefield draw at Antietam—Sharpsburg to southerners—was far more decisive than was seen at the time. The North let slip a strategic victory but denied one to the South: by turning back Lee's invasion the union dissuaded the British and French governments from granting diplomatic recognition to the confederacy. Had they done so, Mr McPherson believes, other European powers, save perhaps Russia, would have followed their lead.

It changed the purpose too

More important still, the confederate withdrawal at Antietam gave Abraham Lincoln the confidence he needed to issue the emancipation proclamation, and so transform the character of the war. From then on the fight for reunion was also a fight for freedom. The Yankees had occupied the

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moral high ground. As Richard Cobden, a prominent pro-union member of the British Parliament, said of the proclamation at the time: "It has closed the mouths of those who have been advocating the side of the South. Recognition of the South, by England, whilst it bases itself on Negro slavery, is an impossibility."

In this book, as in his magnificent history of the civil war as a whole, "Battle Cry of Freedom" (Oxford, 1988), Mr McPherson cannot conceal that his heart lies on the northern side. But even he can scarce forbear to cheer the dash of the confederacy's cavalry and the resilience of its infantry. He recalls the words of a union surgeon at the time: "It is beyond all wonder how such men as the rebel troops can fight as they do; that, filthy, sick, hungry, and miserable, they should prove such heroes in fight, is past explanation."

Mr McPherson's judgments of the relative strengths and weaknesses of the rival generals is as interesting as his account of the battle itself. He characterises Lee as "the greatest risk taker of all"; in fact, almost the precise opposite of the man whom McClellan described in his unintentionally comical assessment of Lee before the earlier Seven Days' Battles: "cautious & weak under grave responsibility...wanting in moral firmness when pressed by heavy responsibility...likely to be timid & irresolute in action."

Instead, Lee became the foremost exemplar of what Mr McPherson calls "an offensive-defensive strategy", and not just because of his natural audacity. Lee believed that in a long war the North's greater numbers, resources and industrial capacity would grind the South down. To forestall this prospect, he tried quickly to gather the South's maximum strength and to score a victory that would drive the ene- ➤

► my to the negotiating table. Lee, of course, failed in this aim at Antietam, and again at Gettysburg when he invaded the North for a second time in the summer of 1863. Under Ulysses Grant, the North in the end waged the war of attrition that Lee feared.

Mr McPherson's analysis of McClellan is just as shrewd, and unusually sympathetic. The Yankee general was, he concludes, a perfectionist in a profession where nothing could ever be perfect. His army was perpetually almost ready to move, but could not do so until the last horse was shod and the last soldier fully equipped. McClellan was afraid to risk failure, so he risked nothing. He consistently

overestimated the strength of the enemy forces (sometimes by multiples of two or three) and used these faulty estimates as a reason for inaction.

Nonetheless, Mr McPherson believes that Lincoln was right in saying that no man could lick troops into shape half as well as McClellan. When an exasperated Lincoln finally relieved him of command, McClellan's soldiers yelled their continuing affection for their sacked hero, and many of them wept unashamedly. He may have been too cautious a general, but he was also a desperately unlucky one in coming up against a lion-hearted army led by a battlefield genius. ■

Biography

Getting it down on paper

We've all heard of Harry Potter. Who nowadays knows about Harry Kessler?

W.H. AUDEN called him probably the most cosmopolitan man who ever lived. Aesthete, patron, diplomat, diarist, peace campaigner, defender of the Weimar republic and exile from Nazism, this ultra-sophisticated German count belongs to a type that probably no longer exists: a moneyed and cultivated amateur whose brains and background brought him effortless access to politics, society and intellectual life in any capital where he set foot.

The diary he kept from the age of 12 in 1880 to his death in 1937 attests to an astonishing range of friends and interests. How can one man have taken so many meals with so many famous people in a waking day? Henry James, who boasted of dining out more than 200 times in a single London winter, seems by comparison like a stay-at-home. Through the pages of Kessler's diary pass Herbert Asquith, Pierre Bonnard, Jean Cocteau, Serge Diaghilev, Albert Einstein, André Gide, Hugo von Hofmannsthal... You could exhaust several alphabets before draining the contents of this extraordinary man's address book.

Kessler was not dropping names. These were his friends, people he kept up with, people he worked with on his countless artistic or political projects, and people he campaigned with for what he believed in. There was more than a touch of vanity in Kessler, and he was certainly a snob. But his hard work and loyalty at making and keeping friends is ever visible.

Kessler is now perhaps most familiar from a portrait of him by Edvard Munch in the Nationalgalerie in Berlin. But the trim figure of a self-satisfied dandy leaning on a cane in a panama is misleading, for it misses the streak of north German seri-

The Red Count: The Life and Times of Harry Kessler. By Laird M. Easton. University of California Press; 512 pages; \$35 and £24.95

ousness in him that hardened as he aged.

In the first full biography in English, Laird Easton describes Kessler's life in detail and well. He is especially strong on the early years and education. Kessler's father was a Hamburg banker, his mother the granddaughter of an Anglo-Irish colonel and a Persian princess. On the promenade at Ems, his mother caught the eye of Wilhelm I, who ennobled her husband, and Kessler spent a lifetime denying that he was the kaiser's son (the dates don't work, and he almost certainly wasn't).

After school in England and Hamburg, Kessler acquired at Bonn and Leipzig universities an intellectual backbone that saved him from dilettantism and gave his diaries their refreshing lucidity and rigour. He joined the right clubs and the right regiment of Prussian lancers, without for a minute sharing their habits or ideals. As museum director in Weimar—his one brush with paid employment—he championed modern art, provoking objections from the volatile new kaiser in person. Following William Morris, he founded a fine press and supported the revolutionary, bare stagecraft of Edward Gordon Craig.

Kessler saw war on the eastern front and at Verdun, where he was invalided away from in shock. Afterwards he acted as a secret envoy in Switzerland for the empire and again in Poland for the new German republic. His eye-witness reports from post-war Warsaw and Berlin are bril-



liant evocations of cities on the brink.

By now a left-wing liberal, Kessler sought an elusive middle way between right and left. A patriot, he campaigned internationally not for German revenge but peace and understanding, though the times allowed scant room for either. Remarkable on these bravely wet commitments, Richard Strauss's wife snapped at him: "A democrat and a count! You're fouling your own nest." Less viciously, you could say Kessler was of politics but not in it, belonging to so many worlds and none. When in 1933, his valet, a Nazi's son, warned him that he was on the party's enemy list, Kessler left Germany for good.

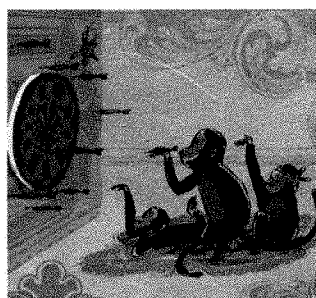
Kessler's actual achievements were few, as Mr Easton acknowledges, particularly when set against his "vast nimbus of potentiality". His friend Hofmannsthal, on whose librettos he collaborated, thought "the decisive element" in him was missing. Luckily for us, Kessler put not his own doubts and complexities but his times and his friends into a remarkable, indispensable diary. Handy editions are in print from Insel (1996) and in English from Phoenix and from Grove (2000). No better record exists of Kessler's vanished world. ■



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Business

The UN's **World Summit on Sustainable Development** opened in Johannesburg. Solid achievement may be hampered by lack of agreement over the precise meaning of sustainable development. AIDS, aid, trade, hunger, poverty, energy, the environment and desultory chatter on the state of the world have all vied for a hearing.

Phone charges

Scott Sullivan, former chief financial officer of **WorldCom**, and another executive, were charged over the accounting fraud that brought down America's second-largest long-distance telecoms company in July.

An American congressional committee investigating **WorldCom's** collapse learned that **Salomon Smith Barney**, now a unit of Citigroup, had allocated hundreds of thousands of shares in desirable initial public offerings to WorldCom executives. SSB admits handing over the shares but denies "spinning", offering valuable shares to win banking business.

Marconi agreed a restructuring that will hand control to its creditors. Shareholders in the embattled telecoms-equipment concern, which was formerly the British company **GEC**, will be left with a mere 0.5% stake.

Andersen Worldwide agreed to pay \$40m to settle a lawsuit brought by Enron shareholders against the auditor of the bankrupt energy trader. Andersen's international affiliates will also pay Enron's creditors \$20m. Andersen's American arm, which was mainly responsible for auditing Enron, was not included; lawsuits against it are still pending.

YTL Power denied paying a bribe of £1m (\$1.5m) to secure the purchase of **Wessex Water**, a subsidiary of Enron, for \$777m this year. Colin Skellett,

Wessex's chief executive, was questioned by British police regarding "corrupt payments". He denied involvement in the sale of the water company but admitted pocketing a £1m in a consulting agreement.

Europe's struggling **mobile-phone operators** are likely to get some respite from the European Commission. Huge sums spent on third-generation licences may be offset if competing telecoms firms are given the go-ahead to share the costs of building networks. Despite this concession, profits still seem far distant.

Siemens is planning to cut a further 4,000 jobs at its fixed-line telecoms unit, some 7% of the total, as part of drastic cost cutting in response to plunging orders for for the German company.

Steel past the guards
Pity America's steel makers. George Bush attempted to mollify the EU by granting exclusions from steel tariffs of up to 30% announced in March. Now America's International Trade Commission has rejected charges of dumping brought by America's steel makers against firms from five countries. The ITC is still con-

sidering the same charges against 15 other countries.

Potential bidders for **Hershey Foods** saw public opposition to the sale reinforced by Mike Fisher, Pennsylvania's Republican attorney-general, who is running for governor. He asked the state's charity regulator, which has jurisdiction over Hershey's controlling charitable trust, to block a sale temporarily to allow time for consideration of the effects on the community.

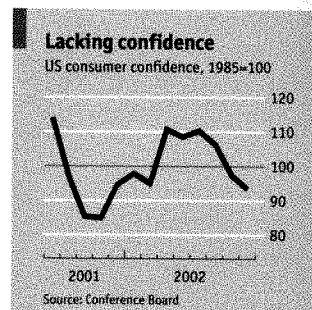
Hewlett-Packard announced losses of \$2 billion for the quarter to the end of July, after taking charges of some \$3 billion related to its recent acquisition of Compaq Computer. Sales in the quarter also disappointed but HP stressed that the economy—not the merger of the two firms—was to blame.

Bank withdrawal

The world of Nordic banking was rocked by the exit of the chief executive of the region's biggest bank, **Nordea**. Thorleif Krarup departed from the post shortly after the bank announced that second-quarter profits had slumped by 66% over a year ago to €91m (\$84m)—but he will remain with the bank.

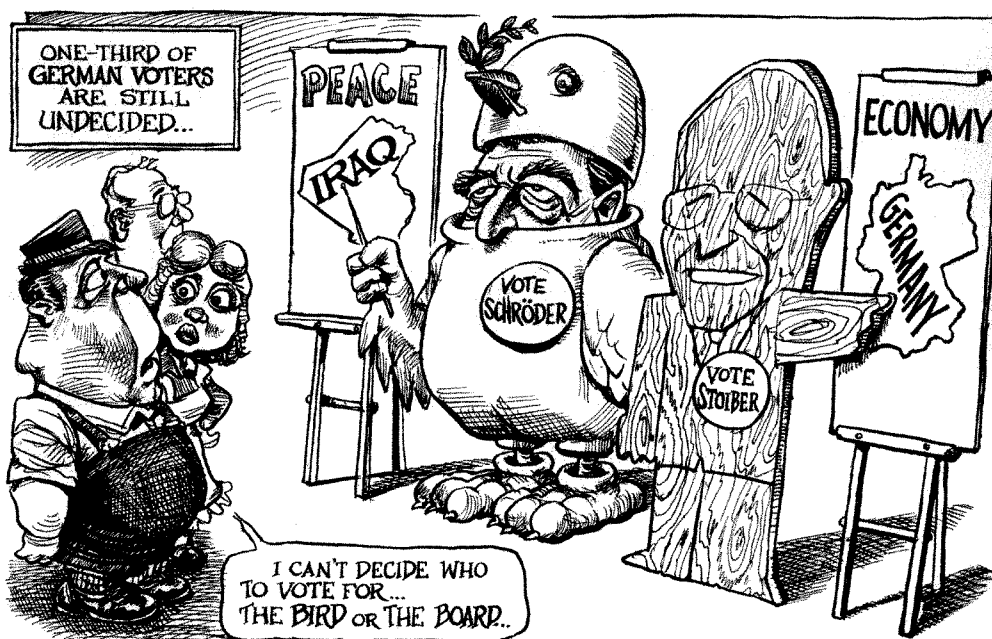
National Australia Bank beat a retreat from the American mortgage market by selling the parent company of HomeSide Lending to Washington Mutual for A\$2.3 billion (\$1.3 billion). The American company had already purchased HomeSide's operating platform and its assets earlier in the year for \$1.9 billion.

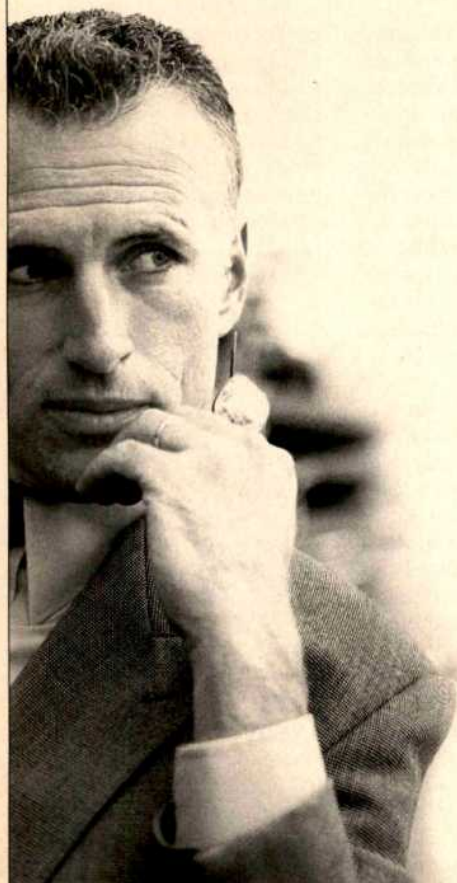
Ups and downs



America's economy suffered mixed fortunes. Durable-goods orders in July surged by 8.7% compared with a year ago. However, according to the Conference Board, consumer confidence continued to fall, to its lowest since last November. **Germany's** main indicator of business confidence also fell in August for a third month in a row.

Other economic data and news can be found on pages 72-74





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Sustaining the poor's development

The biggest environmental gathering in a decade could do some good—but only if it does not overreach



JUST what is the UN's "World Summit on Sustainable Development" for? This giant jamboree, which opened in Johannesburg this week and will culminate on September 4th with a meeting of over 100 heads of government, risks be-

ing about everything and therefore, in the end, about nothing. No one in their right mind is against "sustainable development". Everyone thinks it would be terrific if there were less poverty, less pollution, less disease, less war, less corruption. Not quite everyone, alas, favours more democracy, especially in the poorer parts of the world; in the richer world, too, not quite everyone, alas, favours more economic growth. But the world did not need tens of thousands of people to travel to South Africa in order to learn all of that.

Such a gathering is bound to do some good, simply through the contacts made and ideas exchanged, in myriad small but useful ways. But there are also big dangers in summits such as these. Grand meetings, like the "Earth Summit" in Rio de Janeiro in 1992 to which this was originally meant to be a follow-up, can breed confusion and cynicism. Confusion, because of the cacophony of different voices and objectives, to which this broader summit looks especially prone. Cynicism, because the bold promises made are so rarely met. How many countries have actually hit (or are really on their way to hitting) the targets set at Rio, or in Kyoto in 1998, for cutting greenhouse-gas emissions? Precious few.

Keep the real agenda simple

George Bush has responded to these dangers by staying away, sending his secretary of state, Colin Powell, instead. That was a mistake, offering *carte blanche* for criticism of America for almost any environmental or economic ill, some justified, most not. That is a pity, for America has actually played a more constructive role at the summit than most think (see pages 55-57). Other rich-country leaders can, however, learn from that public-relations blunder. But only if they focus on what really matters, and on what can really be achieved.

The first thing they should do is to tell the truth about poverty, growth and the environment. Thabo Mbeki, South Africa's president, delighted the anti-growth lobby with his opening speech, but did a huge disservice to the facts. "Sadly", he said, "we have not made much progress in realising the grand vision...the tragic result of this is the avoidable increase in human misery and ecological degradation, including the growing gap between North and South. It is as though we are determined to regress to the most primitive condition of existence in the animal world, of the survival of the fittest."

In contrast, what responsible heads of government should say is that the ten years since the Rio summit (home of that "grand vision") have seen lots of progress in enhancing human welfare, especially in the most populous countries of the world, China and India, thanks to those countries' decisions to liberalise their economies and to open their borders to more

trade and investment. Such globalisation has already narrowed the overall gap between North and South. But some countries, notably in Africa and the Middle East, have chosen not to take part in that process, and misery there has increased. Others, particularly in southern Africa, have been so beset by disease that they have been unable to take part. Much more can, and should, be done to help them do so. And measures can and should be taken to ensure that the future economic growth of the poor world, if that happy outcome occurs, does not unduly exacerbate the problem of global warming.

The second thing that western leaders can do is to state clearly what they can, and cannot, do for their poorer counterparts. They cannot "share assets more equitably", as some claim; making the rich poorer will not make the poor richer. Virtually everything needed to help countries grow and reduce poverty depends chiefly on domestic policies—ask South Korea, China and even India. Western leaders can still, however, be helpful, in two powerful ways. They can open their country's markets to the goods that many poor countries are best suited to produce, namely food and textiles. And they can focus their overseas aid on the issue that is most difficult for poor countries to deal with themselves: disease.

There are signs that the summit could achieve something on both fronts. Farm subsidies are properly the domain of the new round of world trade talks launched in Doha last November, but are also a source of much hypocrisy. It is outrageous that rich countries preach free trade to the poor while lavishing over \$300 billion a year on their own farmers. Despite its recent increase in production subsidies (to levels still below Europe's), the United States recently put forward a welcome long-term proposal for reducing subsidies for agriculture, much pooh-pooed in Europe. The Johannesburg summit offers a fresh opportunity to embarrass the Europeans into taking the proposal seriously, and to get all sides committed to a broader dismantling of subsidies in the Doha round.

On disease, too, progress could be made. The scourge of AIDS is debilitating African economies, as are other diseases such as malaria and tuberculosis. More broadly, dirty water and air, and poor sanitation, are the biggest preventable causes of death. Faster economic growth would help poor countries solve those problems. But disease itself thwarts that growth. There has been much useful talk at the summit of agreements between businesses, aid organisations and governments to try to fight against disease, in ways both big and small. The anti-business lobbyists may not like it, but the UN has been right to encourage such agreements, and rich-country leaders should welcome them too. Better still, they should make further increases in their official aid budgets to take on these diseases, both bilaterally and through global funds.

But what of the environment? Isn't that what this summit was supposed to be about? Yes, but enabling poor countries to grow and be healthier will go a long way towards protecting it. If they want to make one big green gesture, though, leaders could most usefully agree to phase out the subsidies they pay for the dirtiest fuels, particularly coal. That way, both rich and poor can work together to avoid global warming. ■

It is far from clear, though, that many of the Bush administration's actions over the past year will be effective or that they would be justified even if they were. The administration has been much too ready to try to evade both the law and the courts, to act in secret, and to resort to indiscriminate means of oversight and investigation. Its claim that it can designate even American citizens as enemy combatants and thereby hold them indefinitely while denying them the right to a trial is particularly worrying. The American constitution is a flexible document which recognises the possibility of grave threats to the republic. It allows for the suspension of *habeas corpus*. But it does not look kindly on unreasonable searches, secret trials or detention without any trial at all.

Act wisely, or not at all

Terrorism is undoubtedly hideously difficult to deal with, and politicians are well aware that the voters will be unforgiving if they are not seen to be doing something. Some actions, however, are worse than inaction. If every act of terrorism is met by a tightening of security and a concomitant loss of freedom, governments will be giving terrorists an automatic victory with every new outrage. That is not the way John Ashcroft, the

attorney-general, sees it. He argues that "those who scare peace-loving people with phantoms of lost liberty" only aid terrorists. He has things on their head.

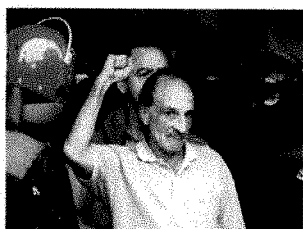
Fortunately, the courts are there to uphold the law, and this week the administration was dealt a sharp rebuff when a federal appeals court ruled it was wrong to hold hundreds of deportation hearings in secret. "The executive branch seeks to uproot people's lives, outside the public eye, and behind a closed door," it said. "Democracies die behind closed doors." It was right. Whatever the need for greater surveillance, no case has been made for abandoning the right to open justice.

Mr Bush may have made a mistake when he chose to call his response to September 11th a "war". Talk of war conjures up the need for the suspension of normal political life and even of civil liberties. That is bad enough in a war of the conventional kind. But this war, if war it is, is one that may go on for ever. It can certainly never be declared won; terrorism, like poverty, is probably always with us. Awful as it sounds, that may mean learning to live with terror, even as you fight it: to be dominated by a fear of terrorists, to credit them with greater power than they really have, and to tear up your freedoms in the face of their threats is to hand them a needless victory. ■

Terrorism in Spain

Batasuna banned

A mistake, even though ETA's political party deserves no sympathy



IT IS not easy to make a defence for Batasuna. Whatever its protestations, it is plainly the political wing of the Basque terrorist group ETA, whose tactics are as nasty as its cause is flawed. ETA wants independence for the Basque region of

northern Spain (and south-western France). It cannot persuade a majority even of Basques that this is a good idea, perhaps because the Basques are not oppressed; indeed they enjoy a high degree of self-government. So it pursues its objective through bombing and other forms of violence. Batasuna itself has not been proved to be complicit in these killings, which have so far claimed the lives of over 800 people, but it does not condemn them. Some of its members are surely members of ETA. Why then should anyone want to defend Batasuna, which was closed down by a court order this week after Spain's parliament had voted to ban it (see page 37)?

They should not. But that is not to say that the banning is wise. For reasons that probably lie in Spain's Francoist (and fiercely centralising) past, Batasuna has quite a bit of support: it took 10% of the vote in the regional elections last year, 18% in 1998. And though violence is not popular, the cause of Basque separatism is: other groups, including many of the mainstream nationalists who run the Basque region, also hope for independence. Batasuna is already casting itself as a victim, unable now to air its opinions legally.

Other considerations too should have counselled caution. In principle, democracies—especially those as young as Spain's—should ban political parties only for outright anti-democratic activity. That has not been established in Bata-

sunas case. Its views may be odious, but free speech should be valued to protect not anodyne views but offensive ones. Moreover, measures short of a complete ban could, and should, have been taken against it. It would have been right to hold it responsible for the damage caused by its young firebrands in their ritual demonstrations. And it could well have been excluded from the taxpayer-financed funds handed out to Spain's political parties.

The circumstances of the ban are also somewhat disquieting. Judge Baltasar Garzon, the harrier of Chile's Augusto Pinochet, has played a leading role, certainly in the closing down of Batasuna's offices, which took place with a considerable show of force. Judge Garzon is anything but publicity-shy. Even the motives of the prime minister, Jose Maria Aznar, are not beyond suspicion. He says that Batasuna is incorrigible, and that his aim is to ensure that people will not be too frightened to stand as candidates of the mainstream parties in the Basque municipal elections next May. But critics point to a vengeful streak in the banning: ETA has tried to kill Mr Aznar (and other leading politicians), and his attempt a few years ago to wrest power from the nationalists in the regional government failed. Some believe he is trying to divide the nationalist camp in order to promote the interests of his own party.

That might not be so terrible if it worked. The worry, though, is that this will do nothing to end terrorism, though it may well make it harder to find a channel through which to talk when the time comes, as surely it must, for political overtures. In truth, the Basque problem will not be solved by repression alone. At some stage, politics will be involved. In a country where it is taboo even to countenance self-determination for the Basques, let alone to hold a referendum, that stage still seems far off. The banning pushes it even further away. ■

Political oaths

SIR – If legislation is the answer to control errant bosses, do you not believe also that elected representatives should be required to swear under oath that they have read the legislation on which a vote is being taken and that it contains no typographical or other errors (“I swear...”, August 17th)? Why not hold them to the same standard they are setting for others? When it comes to innovative accounting, no private corporation can match what America’s government does with its “on-budget” and “off-budget” classifications or its practice of spending cash in trust funds for purposes other than that for which it was collected.

Not a day goes by without revelations of fraud, mismanagement or incompetence in the use of government funds. I would much rather rely on the morality and good sense of most of the business people I know than on politicians, or on the members of the media for that matter.

ROBERT COQUILLETTE
Lexington, Massachusetts

Free trade for the Americas

SIR – You say, in essence, that America should not get distracted with bilateral deals such as free-trade agreements with Chile and Singapore (“Fast track to Doha”, August 3rd). Rather, you recommend that America concentrates on more general agreements such as Doha. You are right about the importance of Doha, and the crucial role that American leadership will have in successfully completing a new multilateral trade round. However, your view about the free-trade agreement with Chile is too narrow. It is important because it is a crucial step towards the Free-Trade Agreement of the Americas (FTAA), which would create a larger free-trade area than the European Union.

FTAA’s target date is only two-and-a-half years away. So far, little progress has been made towards it precisely be-

cause America’s government has lacked fast-track authority since 1994. Now that fast track is back, signing a deal with Chile would signal a renewed American commitment to FTAA. In turn, clear progress towards FTAA would help change expectations about the region, as it would shift attention from Argentina’s crisis and Brazil’s problems to the vision of a more prosperous shared future in the Americas.

FELIPE LARRAIN
Pontificia Universidad Catolica de Chile
Santiago

Other-worldly?

SIR – You are grossly unfair to the “worldly philosophers” we economists are—most of the time (Economics focus, August 17th). My generation (I am not yet in my mid-50s) was taught to value the real-world pricing studies of R.L. Hall and C.J. Hitch from the 1930s (and P.W.S. Andrews over an entire lifetime), who pioneered the activity of “learning by asking” in structured and systematic ways. You also neglect Sir John Clapham, whose visit to a hat factory in the 1920s inspired the great debates about imperfect competition and returns to scale in manufacturing. That Milton Friedman belittled the work of these foot soldiers and shunted the worldly philosophers away from “asking about prices” and “learning by asking” was a tragedy from which we are still to recover.

K. VELA VELUPILLAI
Galway, Ireland

Reply from the Rock

SIR – Alejandro Vigil (Letters, August 17th) alleges that Gibraltar specialises in tax evasion and drug trafficking. It does not. It has been held up as a benchmark jurisdiction for financial regulation by the British government. It has been externally audited and found co-operative and compliant with international standards by the Financial Action Task Force on anti-money-

laundering controls and America’s Internal Revenue Service regarding customer-identification rules. It has given a commitment to the OECD on transparency and the exchange of information. Most recently, the IMF audited Gibraltar’s financial services and found that it complied with 66 out of 67 international standards (the exception, inadequate on-site inspections in the insurance field, is being addressed), remarking that it is “at the forefront of the development of good practices”.

As to being damaging to Spain, Gibraltar’s economy employs several thousand Spanish workers and channels substantial investment to Spain. Mr Vigil’s accusations are a poor attempt at justifying the unjustifiable—the undemocratic nature of the current Anglo-Spanish talks—by tarnishing Gibraltar’s reputation.

KEITH AZOPARDI
Deputy-chief minister
Gibraltar

Muslims in Europe

SIR – Your article on Europe’s Muslims falls into the “them and us” trap that stifles the progress of political thought on Islam (“Europe’s Muslims”, August 10th). Islam is an Eastern import like Christianity but it is neither a sudden nor recent one. Europeans made the first journey to Muslim lands in a campaign of ethnic cleansing—the Crusades. This began a series of exchanges that were not all bad.

Fresh socio-economic, scientific and administrative thinking enabled modernisation in Europe. Muslims have existed in the Balkans and southern France for centuries; Muslim Spain was the equitable melting-pot of which America can only dream. Muslims cannot be understood as an insular migrant minority.

ABU-NUSAYBAH NAVED SIDDIQI
Slough, Berkshire

SIR – As a transplanted Muslim in America, I am grateful to western culture for helping

me liberate myself from all the dogma and orthodoxy that the Koran had forced upon me. Sadly, for most of my family and friends in the West the Koran continues to work like a stop-gap, constantly reminding them that only Allah can engage in critical thinking. As a result, they are trapped in the language of absolutes, viewing the world only in black and white. Also, saddened by exile, they favour the certainties that orthodoxies provide rather than trying to understand how a western democracy works.

SABAH SALIH
Danville, Pennsylvania

SIR – It seems that Europe is not at ease with Islam. Why must Europeans insist that their countries have a monolithic cultural identity and that Muslims should assimilate? Muslim youths should adhere to their religious practices and cultural roots if they wish. The Turkish secular model you mention is the darling of the West although the military establishment oppresses elected Islamists and imposes “secularism” on all and sundry. And before Europe ventures to teach Muslims about sensitivity to multiculturalism, it should look at its own chequered recent past.

MOHAMMED REHAN MALIK
Santa Monica, California

SIR – Your article has a photograph of three Muslims watching a cricket match (“Dim drums throbbing in the hills half heard”, August 10th). They seem as confused as I am. The square-leg umpire is at mid-off and has joined with the bowler’s umpire in giving the batsman “out”. However, it is nice to see the traditions of the English game continuing: the wearing of whites, the reluctance of the batsman to walk and the impending rain.

ANTHONY STARKINS
Melbourne ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James’s Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com

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Duty station: Dili, East Timor.
Application deadline: 10 September 2002.
Starting date: 30 September 2002.
Duration: 1 year.
Project title: "Strengthening Parliamentary Democracy in East Timor".
Contact: beate.bull@undp.org

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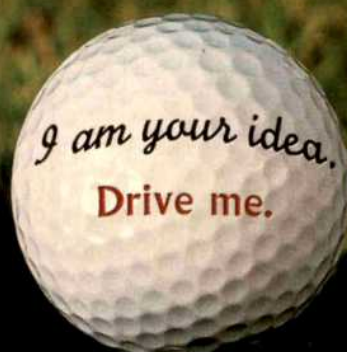
The project manager is expected to:

- Sensitize the stakeholder groups within and outside the parliament to the project objectives;
- Prepare annual and quarterly work plans in close consultation with the National Project Director and the UNDP Programme Officer;
- Implement and monitor project activities to achieve the anticipated results;
- Ensure implementation of the decisions made by the Project Steering Committee;
- Use networks to identify needed expertise;
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Almost everywhere, governments have taken September 11th as an opportunity to restrict their citizens' freedom

FROM the outset, the struggle against al-Qaeda was cast by George Bush as a war for freedom, and for most people, in most places, the 350 or so days that have passed since last September 11th will not be associated with any noticeable diminution of their freedom. For most Afghans, and especially Afghan women, they will surely be associated with liberation. For a few people, though, the aftermath of September 11th has brought unfair arrest, detention without trial, enforced expulsion or some other form of intrusion or repression. Even for those not directly affected by al-Qaeda's attacks, the war in Afghanistan or the anti-terrorism measures taken almost everywhere, the past 12 months may yet come to be seen as an *annus miserabilis* as far as freedom is concerned.

The reason is that, from motives good and bad, governments everywhere have been restricting rights or enforcing existing laws more harshly, and thus reducing the freedoms that people used to enjoy. This is not to say that they have always been wrong to do so: most people in a democracy are quite willing to suffer the inconvenience and invasion of privacy that come with a search of their bag or briefcase when they board an aircraft or enter a public building. Indeed, they might well be worried if they were as free and unimpeded in such places today as they had been a year ago. But their freedom has been curtailed nonetheless and, taken together, many such minor infringements of

freedom, coupled with the precedents they create, may add up to a considerable loss of liberty.

In the United States, where the concept of freedom is built into the very idea of what it means to be an American, and where freedom is therefore never taken for granted, any attempt to reduce it is stoutly resisted. Even so, attempts there have been. Those that have caused most concern to civil libertarians fall into one of three categories. First are the administration's attempts to circumvent the law. "Bush, Ashcroft [the attorney-general, John Ashcroft] run roughshod over Bill of Rights," says a study by the Cato Institute, a conservative Washington think-tank, a sentiment echoed by other watchdogs.

One example is the government's contention that "enemy combatants" have no rights to the due process of American law—meaning they can be denied access to a lawyer and may be detained indefinitely without trial—and moreover that the president can designate even American citizens to be enemy combatants. That is what Mr Bush has done in the case of Yaser Esam Hamdi, a Louisiana-born man captured with the Taliban forces, then transferred to the American base at Guantanamo Bay in Cuba and now held on a naval brig in Norfolk, Virginia.

Both in his case and in that of Jose Padilla, another American, this one arrested in Chicago on suspicion of involvement in an al-Qaeda plot to set off a "dirty" bomb, the

government's motive seems to be a desire to avoid civilian trials. That is thought to be because of the fierce defence put up by John Walker Lindh, an American who fought for the Taliban, and the bizarre course of the trial in a federal criminal court of Zacarias Moussaoui, accused of being al-Qaeda's 20th hijacker. If the government gets its way, though, it will be able simply to lock up enemy combatants, even Americans, without the bother of a trial. Mr Bush has already called Mr Padilla (also known as Abdullah al Muhajir) a "bad guy" and "a threat to the country who is now off the street, where he should be." Donald Rumsfeld, the defence secretary, has said, "We are not interested in trying and punishing him at the moment. We are interested in finding out what he knows."

Rules are for ignoring?

A similar desire to escape legal obligations seems to lie behind the government's eagerness to bypass extradition procedures when it has transferred people suspected of links to terrorism from one country to another, neither of them the United States. Typically, such people—the numbers are unknown—will have been picked up in a country like Indonesia on CIA advice and then taken to a country such as Egypt or Jordan where they can be interrogated using procedures, including torture, that would be illegal in the United States.

A dislike of tiresome rules was also evident in the government's early reluctance to consider the (now) roughly 600 fighters held in Guantanamo Bay to be prisoners of war under the Geneva conventions. It can be seen even more clearly, though, in Mr Bush's order authorising military commissions to try suspected terrorists. Critics are appalled not just that the order betrays a profound lack of confidence in the criminal justice system, but that it also gives the president the unfettered discretion to se- ➤

▶ lect those who will be tried by military tribunal. He will also be the ultimate decision-maker in any appeal.

The second general category of concern about the government's anti-terror measures since September 11th is the secrecy in which they have been taken. The Cato report accuses the administration of "supporting measures antithetical to freedom, such as secretive subpoenas, secretive arrests, secretive trials and secretive deportations." Human Rights Watch, which keeps vigil over civil liberties from New York, reported two weeks ago that "Some 1,200 non-citizens have been secretly arrested and incarcerated in connection with the September 11th investigation... Turning the presumption of innocence on its head, the Department of Justice kept [752 of them] in detention until it decided they had no links to or knowledge of terrorism... Most were ultimately removed from the United States." Jill Savitt of Human Rights Watch worries that because so much has happened in secret, it has all been done with little public debate.

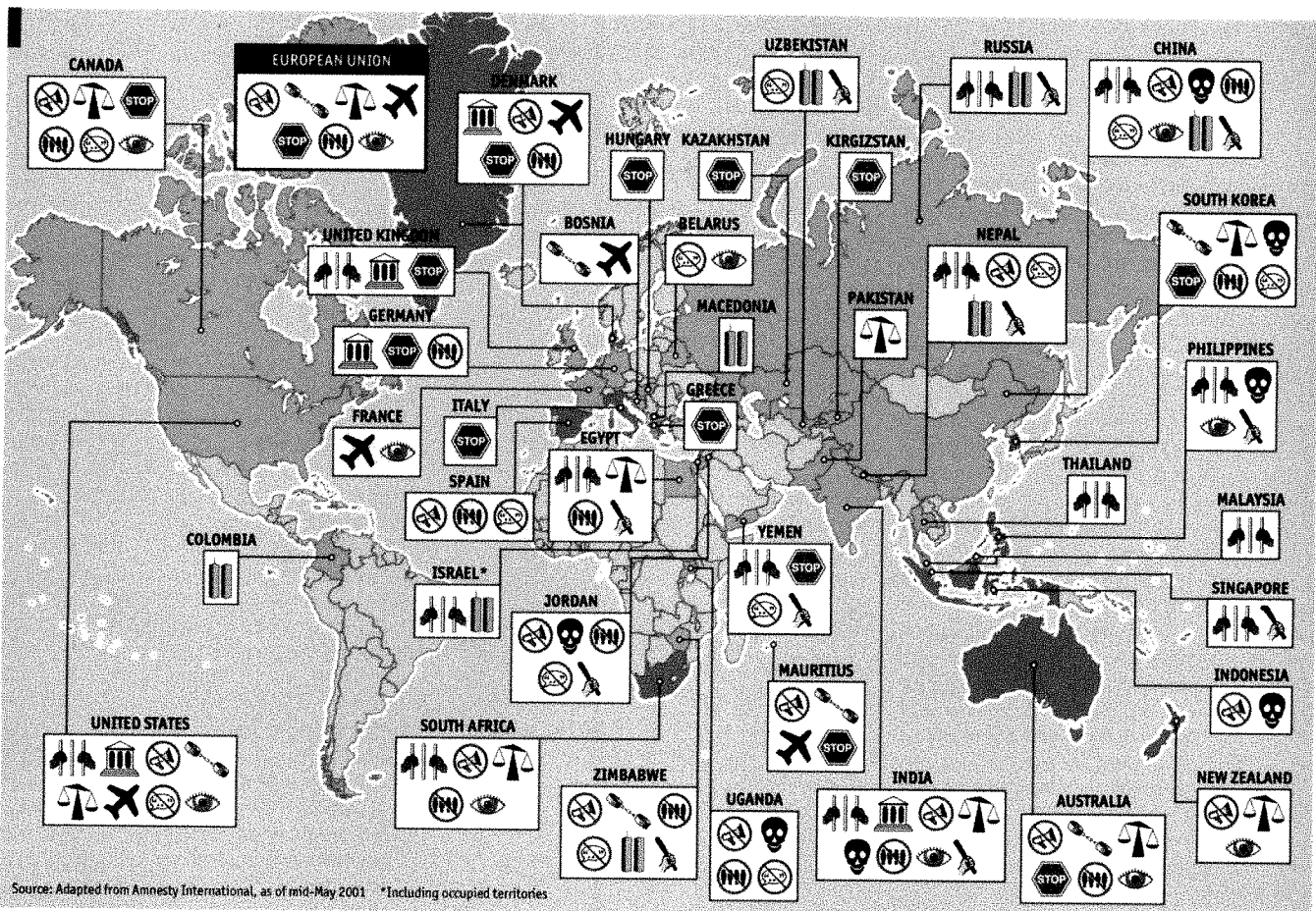
The third area of concern is the sinister nature of some of the wider measures now being taken in the war on terror. Not surprisingly, Arabs have come under close scrutiny over the past year. Despite denials of racial profiling, the authorities stand accused of going after Muslims and Arab-Americans indiscriminately through programmes like the FBI's systematic interviewing of 5,000 people of Arab descent.

Looks funny

In truth, it would be odd if the FBI were not at work among Arab-Americans, but the need to take great care should be apparent from the lessons of history. It is now well recognised that much injustice was involved in campaigns against communists and anarchists after the first world war, in the internment of over 110,000 Japanese-Americans during the second world war and in the McCarthyite witch-hunts at the start of the cold war. Such things could never happen again, some may argue. Yet the administration has been eager to start TIPS, a Terrorism Information and Preven-

tion System in which millions of citizens will be asked to spy upon one another and send their tidbits to a central database. Recent legislation will allow the police to demand records from any business about any person, including medical records from hospitals, educational records from universities, even the reading tastes of shoppers in bookshops and borrowers from libraries.

Americans, of course, are not alone in having seen their freedoms reduced recently. Most countries have taken the opportunity of September 11th to tighten up in the name of security. Common to most of these efforts, as to many of the anti-terror measures recommended by Mr Bush in July, is the long-standing nature of the desire behind them. Often existing legislation has just been extended or amplified. Thus in early June it emerged that the British government wanted to use the Regulation of Investigatory Powers Act, passed two years earlier, to allow countless Whitehall departments, local authorities and other bodies to demand all man-



Areas of concern to human-rights organisations

- Legislation passed after September 11th 2001 - Draft legislation - Previous legislation, enforced after September 11th 2001	- Arbitrary/prolonged detentions - Discriminatory legislation - Clampdown on foreigners/asylum-seekers - Freedom-of-assembly restrictions - Freedom-of-expression restrictions - Increased surveillance powers - Harsher conditions of detention - Erosion of rights at trial - Serious rights violations justified by events of September 11th 2001 - Death penalty expanded - Reported use of torture - Extradition without rights guarantees
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ner of information about e-mails and other communications. The ensuing outcry obliged it to restrain itself somewhat, just as it soon had to rethink its desire to give foreign authorities access to information about British companies. Yet another rebuff came in July when its post-September 11th anti-terrorism act was ruled discriminatory and in breach of human-rights law. The act had given the home secretary powers to detain indefinitely foreigners suspected of terrorism without charging them or sending them for trial.

Buff up the thumbscrews

Most European countries responded to September 11th by rushing through new measures or dusting off old ones to give the police wide powers to investigate and detain suspects. The European Union brought in a long-contested warrant that allows police in one country to arrest people wanted in another for any of 32 crimes, many of them unrelated to terrorism. The European Commission has also proposed much wider definitions of terrorism and what constitutes a terrorist group. Most EU governments have also leapt at the chance to act against asylum-seekers and tighten immigration laws, though their motives in doing so have little to do with security.

They have leapt at other measures too. Thus Spain has moved to ban Batasuna, the political wing of the Basque terror group ETA; Joaquin Almunia, a former leader of the Spanish Socialist Party, says it would have been impossible before September 11th. France has amended its existing anti-terror legislation to allow the police greater freedom to stop and search cars; intended to catch terrorists, the measure is in fact chiefly used to find drugs, says Michel Tubiana, president of the League of the Rights of Man. Another amendment obliges telephone companies and Internet service-providers to keep for a year records of all their customers' communications. In practice, says Mr Tubiana, it is hard to keep only the numbers and not also the content of the messages.

Germany, too, is preparing legislation requiring e-mails and website-address records to be retained. Its internal intelligence agency, the Office for the Protection of the Constitution, has been given direct access to records held by banks, and can now ask the postal service and airlines for information on demand.

On the fringes of Europe, Russia has astutely moved to improve relations with America and, simultaneously, to crack down on the rebels in its secessionist Muslim republic of Chechnya. Despite plenty of evidence to suggest that the long years of fighting in Chechnya have been fuelled by much more than Islamic extremism, Russia has tried to portray the war as little more than an anti-terrorist struggle. Though Chechnya is undoubtedly in-

festes with Islamic extremists, their presence hardly justifies Russia's own terror tactics. Yet Russia escapes censure, certainly from an America now absorbed above all in a global fight against terrorism.

Farther afield, India, emboldened by September 11th, has passed a law that authorises the police to detain suspects for 90 days without trial and to accept evidence from unidentified witnesses. India has long been concerned about terrorist infiltrators from Pakistan. But the real purpose, says Kapil Sibal, an opposition member of Parliament who is also a constitutional lawyer, is to use "this draconian legislation" against India's own citizens.

Hong Kong's anti-terror proposals, which define a terrorist act as one involving the use or threat of force to influence a government, have also been criticised as being so vague that they could be used against a group as unpolitical as the Falun Gong cult. Critics also worry about the power given to Hong Kong's chief executive, who can, for example, freeze the assets of anyone he considers, with "reasonable grounds", to be a terrorist.

Much worse has happened in mainland China, or rather in its province of Xinjiang. There the government has long been persecuting Muslim Uighurs who have protested at the discrimination they suffer and at the policy of swamping them with migrants from other parts of China. In the past, though, the authorities were at pains to play down the Uighurs' protests. But since September 11th the Chinese have deemed it geopolitically correct to admit to the discontent and describe it as terrorism. Indeed, they claim that 1,000 Chinese Muslims have been trained in Osama bin Laden's camps in Afghanistan. Astonishingly, America this week obliged China by declaring a Muslim separatist group to be a terrorist organisation. Amnesty International had earlier reported thousands of political prisoners, torture and summary executions, with an intensification of the

"strike-hard" anti-crime campaign leading to executions among alleged Uighur nationalists. A new wave of executions started after September 11th, it said.

Similar tales come from the new states of Central Asia. The threat of Islamism there has been used to justify ever greater repression by presidents such as Nursultan Nazarbaev of Kazakhstan and Askar Akaev of Kirgizstan, who are squelching dissent as they entrench themselves in power. The sad truth is that September 11th has given despots everywhere a licence to brand all their critics terrorists and take action accordingly. The United States, which anyway needs the help of men like Mr Akaev to prosecute its war against al-Qaeda, is often disinclined to criticise, partly because some of the measures are directly modelled on American ones. Indeed, in a hideous piece of Grand Guignol inspired directly by Mr Bush's actions, President Charles Taylor of Liberia has declared three of his critics (the editor of a local newspaper and two others) to be "illegal combatants". They would therefore be tried for terrorism in a military, not a civilian, court, ruled Mr Taylor.

The widening crack

If all this reads like a tale of woe, no wonder: that is what it is. The world is undoubtedly less free than it was on September 10th last year. Most of the blame for this lies squarely with al-Qaeda. Many governments, it is true, have simply seized the opportunity to pass restrictive measures that they have long coveted. Others, less malign, have undoubtedly been too ready to restrict liberty in the name of an effective campaign against terror: they have reckoned, probably correctly, that the voters would be less forgiving of another terrorist attack made possible by excessive freedom than of the various new restrictions they have imposed. Security is uppermost in the minds of citizens these days, and the true price of an erosion of freedom becomes apparent only over time, which is to say after the next election.

But spare some sympathy, if you can, for the politicians. Some values—good values—are to some degree always at odds with each other, which means that governments must try to balance them. Freedom and security are two such values, even if the trade-off between them is not as simple as politicians often try to claim: a loss of freedom does not necessarily bring a commensurate gain in security.

Do not despair. Though restrictions, once in place, are always difficult to dislodge, and governments are usually loth to give power back to the people from whom they have taken it, freedoms lost can nonetheless be regained. If they are not, however, Mr Bush's fine words last September will have simply served to widen for ever the crack in the Liberty Bell. ■





November could be chilly

China's leadership quarrel

BEIJING

Graven images, Mao, Deng (left) and Jiang, followed by...?

IN AN unusually important but typically bland announcement on August 25th, China ended months of uncertainty by naming the date for the start of its 16th Communist Party Congress. Held only every five years, the congress is where the party's (and thus the country's) top leaders are formally selected, and where broad new policy proposals are launched. The sessions are usually held in September or October, and the delay in planning this year's event gave rise to speculation, among citizens and analysts alike, about infighting at the highest levels of Chinese politics. Now everyone can mark their diaries: the session will begin on November 8th and, state television assures, "all preparatory work for the congress is progressing smoothly at present".

The suspense, however, is far from over, as little is yet known about who will be staying or going. There had been for years an implicit understanding that the party chief, Jiang Zemin, would use the 16th congress to step aside gracefully and make way for a man long ago anointed as his successor, Hu Jintao, vice-president and fellow member of the Politburo Standing Committee. Indeed, having reached the age of 76 and after serving for 13 years as China's top leader, Mr Jiang is at the point where many politicians would start gathering their papers and scouting out book contracts for their memoirs.

Instead, Mr Jiang appears to be scout-

ing around for ways to hang on to power. He holds three posts: state president, head of the Communist Party and chairman of the Central Military Commission, which in effect makes him commander-in-chief of the armed forces. He will have little choice but to give up the presidency early next year, since he will by then have served the maximum of two five-year terms specified by China's constitution. Keeping his military job will be easier. His predecessor as paramount leader, Deng Xiaoping, held on to that job for more than two years after leaving all his other posts, and finally gave up his de facto leading role in Chinese politics only when disabled by old age and senility. However much Mr Hu and the other up-and-coming leaders would prefer Mr Jiang to step aside entirely, the precedent set by Deng will make it hard to object if Mr Jiang follows suit, especially since it was Deng who elevated Mr Hu into the party's top tier.

The key question concerns the party job, which Mr Jiang had been expected to yield to the 59-year-old Mr Hu, in order to comply with an unofficial but widely publicised prohibition on renewing the terms of leaders above 70 years of age. By allowing Mr Hu to meet visiting top-ranking foreign dignitaries and make high-profile official trips to Europe, Asia and the United States, Mr Jiang appeared to be grooming him for the expected promotion. But at the same time, Mr Jiang has refrained from

making any public commitment to standing down. On the contrary, he has in recent months been orchestrating, or at least tolerating, a series of letter-writing campaigns within the bureaucracy aimed at building support for a "Keep Jiang" movement. State-run media, which are mostly under his control, have also been singing Mr Jiang's praises in what looks like an effort to portray him as indispensable.

But others have been writing as well, and in decidedly contrary tones. Bao Tong, a former official who was the highest-ranking figure to be jailed for supporting the 1989 Tiananmen Square protest movement, this week released a stinging essay attacking the "three represents" concept put forth two years ago by Mr Jiang to help keep the party in tune with China's fast-changing social and economic landscape. Mr Jiang calls on the party to represent "advanced productive forces", "advanced culture" and "the broad interests of the public". According to party sources, Mr Jiang hopes to insert the "three represents" into the party constitution at the forthcoming congress; he may also seek to put it into practice by allowing wealthy private businessmen—undeniably the leaders of China's "advanced productive forces"—to hold high-level party posts.

In his essay, Mr Bao, who was a leader of the liberal reform faction that was purged after the turmoil of 1989, writes that the party represents only its own interests, and offers nothing to China's peasants and workers who were promised the moon in 1949 when the Communists came to power. Speaking on the phone from his Beijing home, where he lives under constant surveillance, Mr Bao urged that Mr Jiang should step aside entirely. He rubbished the notion that Mr Jiang should stay on for the sake of stability. "If China's stability actually depends on any single

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person, then the situation must be very dangerous already, and very tragic."

Of course, the possibility remains that Mr Jiang intends to step down after all. Some analysts suggest the congress has been delayed so that Mr Jiang would remain the nominal top leader when he makes his proposed visit to George Bush's Texas ranch in late October. He may also be withholding his decision to retire as a bargaining chip to elevate his chief protégé, Zeng Qinghong, to a place in the Politburo. Mr Zeng is hugely unpopular within the party. David Bachman, an American China expert, says that if Mr Jiang stays on, or merely succeeds in elevating Mr Zeng against the opposition of virtually every other top leader, the result will be instability among the political elite deprived of orderly succession. But if Mr Hu is allowed to move up as planned, it will demonstrate a level of political maturity that the West should give it credit for. That may serve as a more profound political legacy for Mr Jiang than the "three represents". ■

India and Pakistan

A war in waiting

DELHI

Looking beyond October

WHEN Richard Armitage, the United States deputy secretary of state, visited India and Pakistan at the end of last week, he said that tensions between the two nuclear powers had "eased". But L.K. Advani, India's deputy prime minister, was reported as saying at the same time in London that "we are at war"; and this week Yashwant Sinha, India's foreign min-

ister, refused to agree with Mr Armitage's assessment. So is there a risk of returning to the situation of May, when there was a widely perceived risk of war?

Militarily, the situation remains grim. Hundreds of thousands of troops are mobilised on the border between the two countries in a stand-off that started eight months ago, after a terrorist attack on the Indian Parliament. There is shooting across the UN-negotiated "line of control" (the de facto border in Kashmir) almost every day, and Pakistan accused India during Mr Armitage's visit of bombing one of its army posts high in the Ladakh range of the Himalayas (which India denied). Meanwhile, India accuses Pakistan of continuing to send and support infiltrators who cross the border to commit terrorist attacks in Indian Kashmir, despite pledges by Pakistan's president, General Pervez Musharraf, that this would be stopped.

The short answer however is that, barring a major Pakistan-aided terrorist attack, there is no likelihood of a war, nor of any escalation of hostilities, before elections take place in India's state of Jammu & Kashmir between mid-September and early October. India wants to keep the run-up to the polls as peaceful as possible in order to encourage a reasonable number of people to vote. If the polls are not disrupted by Pakistan-aided militants, India is expected to withdraw some of its troops from the border and it may also agree to peace talks with Pakistan.

It would probably also make its first real attempt for many years to deal with Kashmir's internal problems, notably by discussing the transfer of some central-government powers to the state. But if there is widespread disruption, the government would come under heavy political pressure to take military action across the border.

General Musharraf will be aware of In-

dia's hopes. But he has his own parliamentary elections in October and cannot be seen to be going soft on India. He does not want the Kashmir elections to be peaceful and lead to the constructive domestic moves by India that might follow. So Indian analysts believe that the risk of Pakistan-aided disruption is high. There are reports in Kashmir that infiltration across the border has increased in recent weeks, though it remains much lower than earlier this year.

Mr Armitage could therefore reasonably claim in Islamabad that "clearly the tensions and the rhetoric are somewhat down at present", an assessment that enabled him to praise General Musharraf and secure his continued support for America's primary aim of pursuing al-Qaeda in Pakistan. But for Mr Advani and Mr Sinha, India is in a war, although, as Mr Advani said in London, a war against infiltration and terrorism, not, at least for the present, the sort of war that the countries fought in 1965 and 1971. ■

Afghanistan

How to rebuild a country

New thinking by the Americans?

WHILE the United States is mulling over what to do with Iraq, Afghanistan provides a case study of the difficulties of providing a stable alternative to an undesirable regime—and how much the Americans are willing to contribute to the messy business of reconstruction. After appearing to be interested primarily in hunting down the last of the Taliban and al-Qaeda, are American defence officials now warming to the idea of so-called nation-building?

Donald Rumsfeld, the American secretary of defence, said this month that the real problem in Afghanistan was not security but the fact that not enough aid was being delivered to Hamid Karzai's government. He said American troops would now focus less on security and more on civil work. In an interview with Britain's *Daily Telegraph* this week, Paul Wolfowitz, Mr Rumsfeld's deputy, said there were now no large concentrations of al-Qaeda forces in Afghanistan and that he thought America's focus was shifting to training the Afghan national army, and supporting the International Security Assistance Force (ISAF) and reconstruction efforts.

You cannot reconstruct without money. Mr Wolfowitz, like his boss, is no doubt worried about the lack of it arriving in Kabul. According to Kofi Annan, the UN ►►



India may ease Kashmir's burden

secretary-general, lack of money is undermining the government's efforts to provide basic services and extend its authority beyond Kabul. In January, various countries promised to provide \$4.5 billion for the reconstruction of Afghanistan, \$1.8 billion of which was supposed to be disbursed this year. But according to Abdullah Abdullah, Afghanistan's foreign minister, about 80% of the aid received so far has been for humanitarian work and very little for reconstruction. And although international agencies work closely with the government, little money is going to the government itself. The Afghanistan Reconstruction Trust Fund, managed by the World Bank, is supposed to help the government cover its \$460m current budget but had received less than \$70m by the beginning of August.

The United States, anyway, has been generous. It has pledged \$297m for reconstruction in Afghanistan this year, the bulk of which is being channelled through the State Department's international-development agency. America is by far the largest contributor to a UN appeal for Afghanistan, half of which covers humanitarian matters.

If the Americans are to be faulted it may be that they are complacent over security. Compared with the past 23 years of civil war, security may indeed have taken a turn for the better, but Afghanistan is hardly a haven of peace. It has proved difficult to hunt down the remnants of the old regime. The latest coalition operation, dubbed Mountain Sweep, which ended on August 25th, has produced little more than the usual bounty of weapon caches. There are regular rumours that Mullah Omar and Osama bin Laden may still be alive. Mr Abdullah says he believes Mr bin Laden to be alive and kicking in Pakistan. Warlords compete for power. Two Afghan ministers have been shot dead recently.

The ISAF, whose mandate expires in December, is restricted to Kabul. In March, when the renewal of the previous mandate was discussed in the UN Security Council, James Cunningham, an American envoy, made it clear that his country did not see the need for an expansion beyond the capital. It may now be that the United States, which does not contribute troops but provides logistical support, is no longer against an expansion in the force's scope and size.

Even so, serious obstacles would remain. Most countries are unwilling to provide more troops. Turkey agreed to take over the leadership of the force from Britain on condition the mandate would be limited to Kabul and with promises of money. According to Mr Wolfowitz, finding someone to take over when the Turks leave in December is no easy task. The case study of reconstructing a country is coming up with many far-from-easy tasks. ■

New Zealand

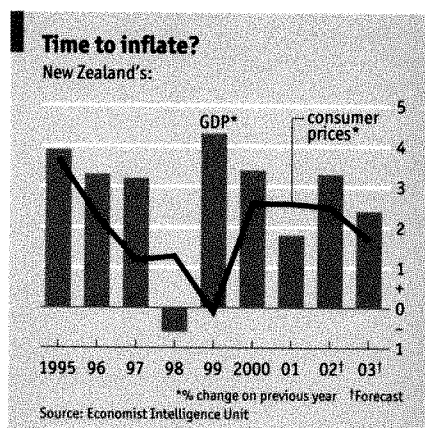
From Brash to Bollard

WELLINGTON

A new man for the bank

IT'S most important decision since winning re-election in July, New Zealand's government has chosen Alan Bollard as the next governor of the central bank. He replaces Don Brash, who for 14 years fought the beast of inflation and brought it to its knees. New Zealand's economy, ranked sixth in income per person in the OECD in 1970, had been so battered by inflation in the 1970s and early 1980s that it had slipped towards the bottom of the table by the time Mr Brash took over.

Yet successful though he was, the country still lagged economically. Australia's average growth in 1990-2000 was 4.1%, compared with New Zealand's 3%. So what was New Zealand doing wrong? One theory was that Mr Brash was over-vigilant about inflation, squeezing not just inflation but the economy. Every time economic growth was heading past 3%, he slammed on the monetary brakes: as he saw it, the country's resources were at full stretch and inflationary pressures were building dangerously.



The finance minister, Michael Cullen, wanted New Zealand to follow the more relaxed strategy of Australia's central bank. The Labour government said it aimed to return New Zealand to the top half of the OECD rankings, raising output per person from something like \$13,000 to \$20,000, Australia's current level, a task that could take years, even based on real growth of 4% a year. Mr Brash, believing that the government was fooling itself, quit his job at the bank and joined the opposition National Party, which crashed to its worst defeat in the general election on July 27th. Mr Brash, though, was elected to Parliament and is the party's finance spokesman. Now Mr Bollard, a public servant who writes novels (unpublished) and ▶▶

Philippines

The hornets are disturbed

MANILA

Surprise decision by the United States

THE Communist Party of the Philippines and its guerrilla arm, the New People's Army, are a relic of the time when Maoism was a threat in Asia. In the Philippines it isn't, much. These days the guerrillas appear to be inspired less by Maoist ideology than by the collection of "revolutionary taxes", which is their main occupation. In other words, they run an extortion racket, and the money goes into their own pockets. This month, to the surprise of many in the Philippines, the United States branded as terrorists the Communist Party and its guerrillas. The belligerent reaction of the party leaders suggested that the American action might breathe new life into their feckless Maoist revolution.

The party's chief peace negotiator, Luis Jalandoni, who is in exile in the Netherlands, said a resumption of peace talks with the Philippine government would be subjected to "indefinite study". A Communist spokesman in the Philippines threatened guerrilla attacks

on American targets in the country. The United States has begun providing money, equipment and training to the Philippine armed forces for their campaign against the Abu Sayyaf, a group of a few dozen armed Filipino Muslim kidnappers. The Abu Sayyaf has also been named by the United States as a terrorist organisation, because it once had links with Osama bin Laden.

The Philippine armed forces could use the American military aid in their operations against the Communists. But the Philippine government ridicules the notion that the New People's Army, estimated by the armed forces to number about 11,000, could ever take power by force of arms. It remains hopeful for a peace agreement. This might still leave the guerrillas armed and collecting "revolutionary taxes" in the wilder parts of the Philippines. But once their leaders have made peace, the guerrillas will become simply a criminal problem, rather than a political one.

likes inventing board games (yet to become popular), jumps from being the government's chief economic adviser as treasury secretary, to the role of the economy's conscience as the central bank's governor.

Economists have been noting Mr Bolland's eagerness to push monetary policy more into line with that of the Australian central bank (which is directed to keep inflation within a 2-3% band). They believe he will go for a little inflation, getting the government to agree to raise the present target band of 0-3%. He has to proceed cautiously, so as not to frighten the markets.

Mr Brash says any relaxation of the target band would be only a cosmetic change. He may have a point. More ruthless action may be needed to boost New Zealand's low productivity. That would call for more than just a culture change at the bank. ■

Malaysia

Threat of the cane

Immigrant workers are needed, but no longer wanted

SINCE an amendment to Malaysia's immigration laws came into force this month, illegal immigrants are being handled with a severity that has drawn protests from neighbouring states. The amendment says that foreign workers without permits, and anyone who employs or harbours them, may be fined up to 10,000 Malaysian dollars (\$2,600), imprisoned for five years and given up to six strokes of a rattan cane. When the amendment was adopted in April a grace period of four months was given to allow illegal immigrants to leave the country. About 300,000, half the estimated number of illegals, have left.

Now the crackdown has begun. On August 10th, seven men, five Indonesians and two Bangladeshis, were jailed and caned after being found without work permits; many more await prosecution. Other illegal workers and their families are being herded into detention centres for deportation, and at least three Filipino children are reported to have died as a result of unhygienic conditions in camps in the eastern state of Sabah.

On August 26th, after stories of the clampdown reached Indonesia, around 40 protesters in Jakarta burned the Malaysian flag and tried to break into the Malaysian embassy. Next day, the Philippine foreign secretary, Blas Ople, complained that, though his country did not expect "Hilton-standard treatment" for its nationals, conditions in detention centres were too harsh. The two countries say they do not

Traffic in children

The camel jockeys of Arabia

Smuggled from Pakistan and Bangladesh

FOR Shabir and Mustafa, both eight years old, their camel riding days are over. Abducted from Pakistan a few years ago, they were smuggled to the United Arab Emirates (UAE) to become camel jockeys. Last month, they were rescued by the Ansar Burney Welfare Trust, a Pakistani NGO, which is now trying to find their parents. Many more are not so lucky: according to the trust, 30 boys—most of them under ten—are being kidnapped in Pakistan every month. A Dhaka-based NGO estimates that over 1,600 Bangladeshi children have been smuggled to the UAE during the past decade to ride camels.

This may now change. The UAE has finally decided to respect a long-ignored law, passed in 1993, which bans the use of jockeys under 15 and weighing less than 45kg (100lb). The Emirates Camel Racing Federation said it would implement the rule from September 1st, in time for the racing season starting in Oc-

tober. Offenders will face a fine of 20,000 dirham (\$5,450) for a first offence, with jail for repeated offences. Airports and ports are on alert to spot South Asian boys being smuggled in.

Young South Asian boys, sold for as little as \$75, are riders of choice for this popular sport. Many are deprived of food and sleep, to keep their weight down. Tiny jockeys, some less than five years old, are strapped to their mounts to avoid deadly falls, but accidents are common. Human-rights organisations, such as Anti-Slavery, have been complaining for years about the practice. The government of Bangladesh has asked the International Organisation for Migration (IOM) to help send victims home.

Repatriation, however, is only the beginning. According to IOM, the hardest part is to reintegrate these young boys who, like Shabir and Mustafa, may have forgotten their families and mother tongue after years in the Gulf.



have the resources to accommodate the homecomers: 200,000 have arrived in Indonesia, and 64,000 in the Philippines. At least 17 people have died while stranded in an overcrowded and unsanitary camp in Indonesia's East Kalimantan province, which the Indonesian Red Cross says holds around 17,000 of the expelled.

In Malaysia employers are saying that mass deportations will damage the economy. The country has long relied on foreign workers to do jobs that locals refuse. Unions estimate that 70% of unskilled building workers are Indonesian. Human-rights groups say that the government's

campaign against illegal immigration fails to deal with associated issues such as human trafficking by agents and employers, and the trade in fake documents.

The Malaysian government sees the crackdown on cheap foreign labour as part of a move to promote more capital-intensive industry, and to protect jobs for locals. It claims that illegal immigrants are responsible for the rising crime rate and pose a security risk. Given that many voters appear to share the government's view, the crackdown on immigrants is likely to prove politically expedient, whatever its economic costs. ■



War with Iraq?

Putting his cards on the table

WASHINGTON, DC

This week, the administration took some confusing first steps to explain its Iraq strategy. If it wants allies, it will have to try harder

FOR months, critics and friends alike have been urging the Bush administration to explain clearly why it wants to remove Saddam Hussein. The idea is that it will then be easier to decide whether to support military action when it comes.

This week, the Bush administration began to play its hand. Speeches by the vice-president and defence secretary provided the most detailed justification so far for wanting to get rid of Mr Hussein. The White House then leaked its lawyers' thoughts about the minimal role Congress formally needs to play in declaring war. The result of all this clarification? A chorus of dissent from abroad and a lukewarm reception at home.

The most important step forward was the speech by Dick Cheney to the Veterans of Foreign Wars, in Nashville. He focused almost entirely on one concern: the Iraqi dictator's attempts to build a nuclear weapon (and the regional consequences this might have). If Mr Hussein got a nuke, said Mr Cheney, he "could be expected to seek domination of the entire Middle East, take control of a great portion of the world's energy supplies, directly threaten America's friends throughout the region and subject the United States or any other nation to nuclear blackmail."

In dealing with such threats, Mr Cheney said that military force was the only

solution. Against those who argue that America should rule out pre-emptive action until Iraq actually acquires a nuke, the vice-president retorted: "That argument comes down to this: 'Yes, Saddam is as dangerous as we say he is, we just need to let him get stronger before we do anything about it...' Many of those who now argue that we should act only if he gets a nuclear weapon would then turn around and say we cannot act because he has [one]."

Mr Cheney also dismissed the argument that Mr Hussein's nuclear ambitions can be thwarted by a return of United Nations weapons inspectors. He went through the history of Iraqi subversion of the inspectorate. "A return of inspectors would provide no assurance whatsoever of compliance with UN resolutions. On the contrary, there is a great danger that it would provide false comfort that Mr Hussein was somehow 'back in his box'."

Mr Cheney's speech ought to have clarified the administration's position. It provided concrete justification for removing Mr Hussein (nuclear weapons, not links with al-Qaeda and September 11th). It was hard-headed (America must remove the Iraqi dictator, not because he is evil, but because he threatens the region). And it was about as plain as it could be that military action is the only course open.

But debate raged on, not least because

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Mr Cheney's was not the only message from the administration. Just before the vice-president's speech, Anthony Zinni, a senior adviser to Colin Powell, the generally doveish secretary of state, said the administration should deal with the Israeli-Palestinian conflict first. Meanwhile, another State Department spokesman explained that Mr Powell was not attempting to rally allies behind any military action because none is planned: "there are no war drums to beat." This also seemed to dovetail with Mr Bush's earlier claim to be "a patient man".

From the opposite end of this spectrum to Mr Powell, Donald Rumsfeld explained that he was also uninterested in rallying allies—though for markedly different reasons. "It is less important to have unanimity," said the hawkish defence secretary, "than it is to be making the right decision and doing the right thing, even though at the outset it may seem lonesome." In other words, Mr Bush would not be delayed in attacking Iraq by lack of support.

Which is perhaps just as well, since Mr Cheney's speech on the face of it failed to produce any support—either at home or abroad. After a lunch at Mr Bush's ranch in Texas, the Saudi ambassador left with his government firmly opposing military action. "There is no country in the world that supports [it]," said Crown Prince Abdallah's foreign-policy adviser, Adel al Jubeir. Egypt's president, Hosni Mubarak, said he feared "chaos happening in the region" if America attacked Mr Hussein. And the foreign minister of Qatar, which is home to a big American air base, popped up in Baghdad to decry "American threats" (Iraq's version) or to explain that the tiny emirate "would prefer to avoid a war" (Qatar's).

And Mr Cheney's speech actually ►►

► seemed to strengthen the opposition of Germany's chancellor, Gerhard Schröder. Picking up the claim that a return of weapons inspectors would only raise "false comfort", Mr Schröder argued that this amounted to a change in policy that he could not support: America had given up trying to foil Mr Hussein's nuclear ambitions by inspections and "if the aim changes now, then it's one's own responsibility." Translation: you're on your own.

Virtually all European governments concur. All have said America should make one last effort to get arms inspectors back in before proceeding to military action. Even Britain may be wobbling a bit: a new poll this week showed most Labour voters now believe that Tony Blair should

not support American policy on Iraq.

This sounds as if America is on a collision course with the rest of the world over Iraq. It may indeed come to that. But three reservations need to be expressed. First, the administration has only just begun to make its case more clearly. Mr Bush, who has not weighed in recently, is due to address the UN General Assembly on September 12th. Second, the administration needs to hold off making its case with full vigour until it is nearly ready to launch a military action; otherwise it risks adding frustration to disagreement. Third, Mr Bush may get allied support only on the brink of war, or even after bombing has started. As Mr Rumsfeld insisted, "leadership in the right direction finds followers."

That said, despite Mr Cheney's efforts, the administration still seems oddly reluctant to persuade even likely supporters to back military action. In holding back, Mr Bush's team seems to confirm the general suspicion that it does not give a hoot what anyone else thinks—including Congress. This suspicion was increased by the leaked White House legal opinion. Mr Bush's lawyers argued that he does not need congressional approval before attacking Iraq on three grounds. None looks watertight.

Three steps forward?

First, say the lawyers, military action against Iraq was approved in advance by a congressional resolution after September 11th. Three days after the attacks, Congress gave the president licence to act against whomever he determined was responsible for them. Therefore, if the president is convinced that Iraq helped al-Qaeda, then Iraq can be attacked. (Perhaps real evidence of a connection may yet come to light, but Mr Cheney's speech seemed to indicate that he does not believe it will.)

Second, that the resolution authorising force in the Gulf war, passed by Congress in 1991, still applies. Mr Bush's lawyers say this document enforces UN Security Council resolution 678, which states that "all necessary means" may be used to "restore international peace and security in the area [of Iraq]." Theoretically, say the lawyers, peace has not been restored, so America can still fight for it.

Legal experts are unconvinced. Louis Fisher, author of a book on the growth of presidential war powers, argues that this would appear to mean that Congress has permanently delegated its authority to declare war to another governing body, which it may not do under the constitution. Others note that resolution 678 and the 1991 congressional act concern Kuwait specifically, not the region as a whole.

The third argument is the most basic. Under the constitution, the president is commander-in-chief and can direct American forces on his own, so long as war is not declared. The trouble is that the constitution gives the president power to "repel sudden attacks", but not to commence an offensive war. Thus the crucial question is whether a "pre-emptive" war is offensive or defensive. Mr Cheney seemed to assert the latter: "We realise that wars are never won on the defensive. We must take the battle to the enemy."

This, surely, is only the first stage in a long argument with Congress. Most people still expect Mr Bush eventually to follow his father and get congressional approval; it would force Democrats to back him or risk looking unpatriotic. But was the best way to win them over to threaten to ignore them altogether? Like so many things this week, the administration's diplomacy needs a smoother touch. ■

The budget

A big black hole

Whatever happened to those surpluses?

IT IS a startling reversal. When George Bush became president in January last year, he was looking forward to a \$5.6 trillion budget surplus in the decade to 2011—more than enough to fund his ambitious tax-cutting strategy. Even Alan Greenspan, the cautious chairman of the Federal Reserve, had started to fret about what the government would do with all the surplus revenues filling its coffers. Yet when the Congressional Budget Office released its latest forecasts on August 27th, most of that surplus had mysteriously vanished. The CBO's new ten-year figure is a mere \$336 billion.

This revision reflects, almost equally, higher spending estimates and lower revenue projections. Spending is up partly because of the fight against terrorism, but mainly because budget deficits, now forecast to run until at least 2005, and then lower surpluses thereafter, push up the cost of interest payments on the government's debt.

The most puzzling change, though, is on the revenue side. Tax revenues have plummeted in the current fiscal year, recording the biggest drop since 1946. Some of the fall is easily explained: the recession has inevitably cut tax receipts, and the collapse in share prices has reduced capital gains on which people pay tax. But the revenue fall goes far beyond what was expected: the CBO's director, Dan Crippen, called it "astounding".

Working out what has happened will have to wait until everyone's tax returns are in. But the CBO is, for now, assuming that the shortfall will persist, and possibly even grow. Its concern is clearly shared by the White House's Office of Management and Budget, which only



last month issued markedly more optimistic projections.

Mitch Daniels, Mr Bush's budget director, pointedly chose not to dispute the CBO figures. Instead, he put the best gloss on them, noting that they showed an eventual return to balanced budgets.

That seems disingenuous. Without the Social Security surplus—which, until quite recently, both Republicans and Democrats had pledged not to touch—the budget will be in deficit until 2010. And the now modest surpluses which will follow will themselves vanish if Mr Bush succeeds in making his tax cuts permanent. They are currently due to end in 2010, and tax rates will revert to what they were when the president took office. Nobody in Washington, D.C., seriously expects that to happen. But as the government's financial position deteriorates, Mr Bush may come under increasing pressure to delay, or cancel, those parts of his huge tax-cut programme which have yet to come into effect.



The great food debate

Come on in

SAN FRANCISCO

How bad is American food? And whose fault is it?

AMERICANS are in a pickle over food. Just as a decade of financial optimism has given way to the shocked discovery that people are poorer than they thought they were, so an era of working out in gyms and low-fat dieting has been mocked by reports of the nation's shocking chubbiness and other food-related forms of ill-health.

The figures on fat are striking. The proportion (if not the proportions) of Americans who are obese rose from 15% in 1991 to 27% in 1999. Youngsters show the same trend: 10% of them are now obese. Add in the merely overweight and you cover 60% of American adults and 25% of children. David Satcher, who retired as surgeon general in February, has estimated that obesity contributes to 300,000 of the 2m deaths each year in America. Treating diet-related conditions such as cancer and heart disease cost \$117 billion in 2000.

What to do? The Bush administration has launched a \$190m advertising campaign aimed at making children more energetic. This week, the Los Angeles school board moved to ban the sale of fizzy drinks in its schools. In May, a Californian state senator abandoned her bill to impose a tax of two cents on every can of pop statewide, but others are still pushing for "sin taxes" on burgers and sugary drinks.

The courts have become involved too. Last month, a New Yorker sued four fast-food chains. He had eaten their food regu-

larly in the course of reaching 272lb (123kg) and notching up two heart attacks. The restaurants, he said, had not warned him that his diet might be harmful.

Meanwhile, another battle has broken out within the fad-crazed health industry itself. The traditional low-fat, bran-and-broccoli dieticians have been challenged by another school that advocates high-protein eating. Beef and lobster, they say, are fine, but you have to stay off carbohydrates such as pasta and bread.

Is the American stomach really in such poor shape? By the standards of most of the world, Americans are fairly healthy. Life expectancy continues to rise; it is bettered only by places that absorb far fewer immigrants from poor countries. Despite jeers from Europe about the number of additives and hormones that go into American food, there have been no health scares on the scale of Britain's mad-cow disease.

Yet Americans are surely right to be agitated about their food. There is an overwhelming amount of evidence that their diet is doing many of them a great deal of harm. The "fat-acceptance" lobby is right that you can be heavy and fit; but without exercise, too much weight makes diabetes and other potentially fatal diseases more likely. Independent of the implications of being overweight, diet also plays a role in other illnesses, such as cancers of the bowel, colon and prostate.

There is also a clear social divide. Both

hunger (which still afflicts 10m households in America) and unhealthy excess correlate closely with poverty and poor education. Shops in poor neighbourhoods stock less fresh food (and at higher prices), while fast-food joints proliferate. Poorer people also have fewer parks and playgrounds in which to exercise.

This sounds bad. Yet the food industry is largely giving American consumers (rich and poor) what they want. A pattern of life in which fewer families eat regular meals together, fewer parents remain at home during the day to cook, and increasing amounts of time are spent working or commuting creates demand for convenient, fast food (especially when it is as cheap as it is). Tummy size, then, is largely a side-effect of modern American life—and the choices that Americans make.

That said, there is a debate about how well informed consumers are when they make these choices. Even if you regard the case of the litigious 272lb New Yorker as absurd, America's food industry is particularly powerful and unfettered. In Europe, the most powerful bit of the food-production chain is the one closest to the consumer—the supermarkets. In America, the industry is controlled by food processors. Three facets of the food business are particularly troubling:

- **Misleading information.** Marion Nestle of New York University points out in "Food Politics" (University of California Press, 2002) that blurbs on packaging are highly selective. Breakfast cereals, for instance, come blazoned with information about how their added minerals and vitamins will strengthen young bones; they have less about what the coating of sugar will do to children's teeth and waistlines.

- **Poor regulation.** The power of the food lobby extends to Washington. The agriculture department has a huge conflict of interest. It is responsible both for promoting the interests of farmers and for disseminating nutritional information. The Food and Drug Administration has been restrained by Congress, at the behest of food interests, in its efforts to regulate dietary claims.

- **Schools.** Eating habits formed by children are hard to shake in adulthood: 60% of obese children grow up into obese adults. Fast-food firms often serve as official caterers, while soft-drink firms have installed numerous snack dispensers in schools (especially poor ones), in exchange for providing things like TVs.

Far from representing something new, the current debate about carbohydrates reflects the confusion created when science and marketing mix. While the 1990s fads concentrated on fatty foods and their link to cholesterol, the high-protein dieticians blame starchy carbohydrates. These, they say, produce a rush of sugar in the blood that destabilises the body's regulation of appetite and so lead to overeating.

► This does help to explain one mystery of the past 20 years: why "low-fat" food did not work. The low-fat meals that Americans guzzled down were often packed with refined flour and heavily sugared to give them flavour (which the customers also wanted); people who tucked into them kept on wanting to eat more. The food industry did not rush to alert them to this point; nor did its packaging mention the sugar as clearly as the "low fat".

Yet the more you delve into the issue, the more nuanced it appears. Just as some fatty foods, such as avocados and peanuts, are now thought to protect the heart (not harm it), there are also some sorts of carbohydrates, such as those found in whole grains, that don't encourage appetite. And the newest research seems to imply that people's genetic disposition might matter more than all these things. Variations in the *apoE* gene, for example, may determine your blood cholesterol level more than your diet. And all that is before you

consider things like the amount of exercise people take.

Over the past 25 years or so, Americans have repeatedly jumped at quick-fix solutions for their fast-food habits. In the late 1990s there was a craze for anti-fat drugs, which inevitably led to lawsuits. But in the end nearly all the arguments about food come back to the choices that consumers make.

Americans have got larger because they have chosen (mainly consciously) to eat the way that they do. Millions of them actually eat rather well: these tend to be the richer and better-educated sorts, who go to gyms and buy their vegetables from organic farmers' markets. Their buying power is having an effect: one of the fastest-growing supermarket chains in America is Whole Foods Markets, based in Austin, Texas, which mixes organic vegetables and free-range chicken with a sorcerer's array of vitamin tonics. But, for the moment at least, they are in a clear thin minority. ■

Florida's gubernatorial race

Hurricane Janet in a lull?

MIAMI

Down but not out, the Democrats may yet give Jeb Bush a run for his money

AFTER the Florida election debacle two years ago, local Democrats could hardly wait to get their revenge on Jeb Bush. But with their own primary approaching on September 10th, Florida's Democrats are deeply divided over how to oust the incumbent governor. Janet Reno, Bill Clinton's attorney-general, was meant to be a shoo-in for the party's nomination. But she now faces a strong challenge from Bill McBride, a Tampa lawyer and decorated war veteran.

Ms Reno has campaigned as the more experienced, grass-roots candidate. Earlier this year she appeared to have all but secured the nomination. But Mr McBride, having won endorsements from several local unions and bigwigs, is catching up. Indeed, his people claim that he now trails Ms Reno by just six points—44% to 38%.

Mr McBride has outstripped Ms Reno in the vital area of fund-raising: he has \$1.9m on hand, twice the amount she has. That will give him an important advertising advantage as the campaign enters the home stretch. Another Democratic candidate, Daryl Jones, a state senator, polls a distant third. Meanwhile, Mr Bush is sitting pretty. The governor is ahead in the polls, and has \$5.8m in his coffers.

Many Democrats have a familiar problem with Miss Reno: their hearts will her to win, their heads reckon that she will

never beat Mr Bush. Even leftish Democrats worry that Miss Reno's liberal image will lose votes, especially in conservative rural areas in the north of the state. Her tenure in the Clinton administration was tainted by her handling of the infamous Waco siege, and by allegations that she was slow to investigate alleged wrongdoings at the White House. She was virtually declared *persona non grata* by Miami Cubans after she ordered the return of Elian Gonzalez, a six-year-old who had travelled

to America on a raft, to his father in Cuba.

Mr McBride, by contrast, suffers from a lack of name recognition. Still, Republicans are nervous that his military record and conservative image could have broad appeal. When the Republicans launched their first campaign ads last week, they took aim at Mr McBride, ignoring Ms Reno. The ads questioned his labour credentials, highlighting lay-offs and pay scales at Holland & Knight, the law firm that he headed. Mr McBride wasted no time issuing his own campaign ad, claiming Mr Bush singled him out for attack "because he knows I'd be the toughest Democrat to beat."

Miss Reno remains undaunted. She has run a gruelling, appealingly down-to-earth campaign, driving around the state in her now-famous red Ford pick-up. She has handled the issue of her Parkinson's disease admirably. A nature-lover who grew up in the Everglades, she also has strong backing from environmentalists.

Whoever wins the primary, Miss Reno and Mr McBride have hinted they might team up afterwards on a joint ticket for governor and lieutenant-governor. Two home-grown Floridians might make an attractive package. This week's televised debate between the three Democrats featured a surprisingly unified and effective assault on Mr Bush's record.

Though elected in 1998 as a self-declared reformer who promised to fix the school system and improve child welfare, Mr Bush is now vulnerable on both counts. Florida has some of the largest and most overcrowded public schools in the country. Most Floridians rank education as the top election issue. Yet when the state faced a sudden budget shortfall due to the loss of tourism revenue after September 11th, Mr Bush chose to cut education funds rather than repeal corporate tax breaks.

To make matters worse, a judge ruled earlier this month that Mr Bush's solution—school tuition vouchers—violated Florida's constitution, on the grounds that it involved tax dollars going to religious schools. For their part, the three Democrats support an amendment that would devote funds to reducing class sizes, a measure Republicans oppose.

Child-welfare is a sensitive subject for Mr Bush. The state's Department of Children and Families (DCF) is mired in scandal, after it admitted that it couldn't locate 500 children supposedly in its care. Though the problems at the DCF pre-date Mr Bush's election in 1998, his reform promises sound hollow. He looked embarrassingly out of touch when, earlier this month, he appointed Jerry Regier, a religious conservative, as the new head of the DCF, apparently unaware that Mr Regier was the author of an evangelical essay condoning, among other things, vigorous spanking. Mr Bush can expect to hear even more about that after September 10th. ■



Winning hearts, but not heads

Lexington The fading lure of Camelot

The pick of the Kennedys is having a tough time in Maryland



THE Kennedy name has lost none of its power to captivate. A display of Jacqueline Kennedy's frocks is attracting packed crowds at the Corcoran in Washington, DC. This year has produced the usual crop of Kennedy books and biopics. But is the Kennedy name losing its power to win elections?

A glance at Maryland, where Kathleen Kennedy Townsend, Robert Kennedy's eldest daughter, is trying to climb the ladder from lieutenant-governor to governor, suggests that it is. The election of KKT, as she is inevitably known, ought to be a cakewalk. Maryland is one of the four most Democratic states in the country: Democrats outnumber Republicans by a margin of two to one. Al Gore carried the state by 57%-40%, an even bigger margin than Bill Clinton managed in 1996. The last Republican to win the governorship was the great Spiro Agnew, back in 1966.

Moreover, KKT is heir to the dynasty's political ambitions, with all the glamour and tragedy that that entails. She has her father's looks (thatched hair and a toothy grin); her family's physical vigour (she once climbed the Matterhorn); and her family's access to Hollywood stars (Martin Sheen has campaigned for her). It is impossible to meet her without reflecting that both her father and her uncle were assassinated. But she also comes across as a sensible and grounded person, a mother of four who has been running for the governorship for the past four years.

And yet her campaign is turning out to be a shambles. The past six months have seen her 15-point lead over Robert Ehrlich, a Republican congressman, dwindle to almost nothing. Her performance has been much less assured than his: stammering and full of malapropisms where he has been smooth and articulate. The fact that he is a local boy made good—he grew up in a row house and made it to Princeton University by dint of his brains and footballing skills—has not escaped the voters. Mrs Townsend has irritated local blacks (who make up 28% of the state's population and most of her party's footsoldiers) by ignoring the claims of several plausible black running-mates in favour of Charles Larson, a white Republican who changed sides just before he was selected. Mr Ehrlich chose a black running-mate.

Mrs Townsend is now scrambling to avoid disaster, hiring a new team to galvanise her campaign and sharpen her polemic. She has also called on the services of Robert Shrum, a veteran Kennedy retainer and specialist in the darker arts of politics. The

Democratic National Committee, terrified of losing a safe governorship, is also stepping in. Come Labour Day, stand by for a torrent of negative ads portraying Mr Ehrlich as a gun-toting Gingrichite who wants to bring back slavery.

This fusillade will probably be enough to save Mrs Townsend. But the very fact that she has stumbled in what should have been an easy race has badly tarnished her reputation. A year ago people were talking about her as a future Democratic star, perhaps even a vice-president. (Mr Clinton speculated that one day he would be "knocking on doors for her when she's running for national office".) Now the golden girl is damaged goods—a problem that the Democratic establishment is desperately trying to solve.

The limits of dynasty

Stephen Hess, a political scientist at the Brookings Institution, points out that membership of a political dynasty buys you one step up the political ladder; whether you reach the next step depends on your own abilities. American political history is littered with the sprigs of political dynasties—including three of FDR's sons—who have made it to the first step and then faded.

Mrs Townsend is discovering that a famous name cannot trump local issues. The Maryland voters are dissatisfied with the party that has been in power for more than 30 years. They are angry with the current governor, Parris Glendening, for his haughty style and zigzagging policies. And they are cross with Mrs Townsend for making a hash of her job as crime tsar. Many of her once-praised schemes seem to have crumbled to dust. The *Baltimore Sun* revealed that the juvenile boot-camps that she championed had degenerated into arenas for sadistic beatings, rampant drug use and skyrocketing recidivism. A federal probe is examining whether Mrs Townsend diverted federal money from crime fighting to political campaigning.

The Townsend campaign is also discovering that a famous name cannot make up for lack of personal charisma. Mrs Townsend is not a bad politician: well-informed, tactile and surprisingly nice. But she's just a little bit on the dull side. She gives the distinct impression that she's going through the motions of building a political career—that she's moved by her sense of duty rather than by any real passion.

The Kennedy magic seems to work best when ambition comes wrapped with a bit of roguery. JFK was an obsessive womaniser. RFK was always embroiled in some feud or other. But the rising generation of Kennedys seem to have lost the ability to combine these two qualities. Most of KKT's brothers and cousins have had too much roguery for their own good. Brother Joe abandoned his race for the governorship of Massachusetts amid a messy row with his first wife. Cousin Patrick is struggling to keep his Rhode Island seat because of his habit of getting into public fights. Mrs Townsend, whose nicknames include "clean Kathleen" and "the nun", has too little of it.

It would be a mistake to write off the Kennedys. They have mastered the first art of survival for a political dynasty: having lots and lots of children. You get a sense of the sheer force of their numbers when you realise that Mrs Townsend is not the only clan member running in Maryland: her cousin, Mark Shriver, is trying to get into Congress. One day the combination of genes and local political circumstances will come together to produce another stellar career. But Kennedy-watchers who have hitched their dreams on Mrs Townsend need to think again. ■



Mexico's economy

With Latin America heading south, Mexico turns its horses north

MEXICO CITY

It has avoided "contagion". But for Mexico to prosper, its government needs to ram through far-reaching economic reforms

ONLY a few years ago, Mexico could be counted on to be at the forefront of any Latin American economic crisis. Yet this year, as Argentina's economic collapse and Brazil's financial panic spread gloom across South America, Mexico has barely been scratched. Indeed, there is much talk of Mexico having ceased to be a Latin American economy at all, thanks to its links with the United States through the North American Free-Trade Agreement (NAFTA). But even if that is true, therein lies a new set of challenges for the government of President Vicente Fox.

Mexico has not been entirely unscathed by the turmoil to its south. Its peso lost 10% of its value between April and June, though it has since stabilised. Since April, the risk premium demanded by investors for holding the country's bonds has risen by around 50%, though it remains far lower than in Brazil's case (see chart). This has increased the cost of borrowing for Mexican companies. The rise also reflects worries about a "double-dip" recession in the United States. Though NAFTA helps shield Mexico from Latin American problems, it increases its dependency on its northern neighbour, which takes 89% of its exports. Were the value of Mexican bonds to fall much further, this would call into question the country's "investment-grade" credit rating, which allows American pension funds to invest in the country's assets.

However, there are good reasons to think that Mexico will continue to pass between the raindrops of the latest Latin American storm. Mr Fox's government has kept to the strict fiscal and monetary policies it inherited from its predecessor. Despite the weaker peso, inflation and interest rates are low. The public debt is well managed. Mexico's achievement, says Victor Herrera of Standard & Poor's, a rating agency, is to have created an economy that is sound enough to insulate its credit rating from temporary turbulence or the business cycle.

This freedom from financial upsets should, in turn, ease Mexico's recovery from a recession triggered by the slowdown in the United States. The latest fig-

ures showed that GDP grew by 2.1% in the second quarter compared with the same period last year. While foreign direct investment (ie, in businesses or factories, not financial assets) has slowed in South America, it remains buoyant in Mexico. Last week, HSBC, a British bank, announced that it was buying Grupo Financiero Bital, one of the last remaining Mexican banks in local hands, for \$1.14 billion.

For all that, Mexico's economy suffers from structural weaknesses which Mr Fox has so far been unable or unwilling to address. One challenge concerns the public finances. The central-government budget deficit is 0.65% of GDP, but the figure for the public sector as a whole is almost 4%. Moreover, there is pressure to spend more. Mr Fox has begun to offer subsidies to special interests, such as farmers and the textile industry. Although the government persuaded the opposition-controlled Congress to approve some tax increases last year, it remains dangerously dependent on volatile oil revenues. These account for 37% of the federal government's revenue.

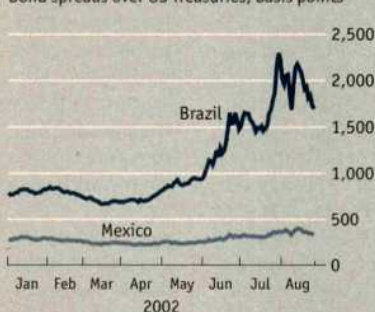
An even bigger challenge has to do with the lack of competitiveness of many of the country's businesses. After 1994's traumatic devaluation rocked the banks, the government allowed a foreign takeover of much of the banking system. But many other business sectors are still tightly controlled by the state or remain private near-monopolies.

In the 1990s, economic growth was led by the expansion of *maquiladoras*, the assembly plants that line the border with the United States. Some of these have now moved deeper south. But as wages rise in Mexico, others have decamped to China. Nobody now expects the *maquiladoras* to match their spectacular growth of the past.

The government hopes that future growth will come from a combination of ►►

Small waves in Mexico

Bond spreads over US Treasuries, basis points



Source: J.P. Morgan Chase

exports and the local market. But for business to remain competitive at higher wage rates, reforms of energy, the labour market and competition policy are all vital. Luis Ernesto Derbez, the economy minister, argues that the government's macro reforms have reduced the risk of investing in Mexico, and that the task now is to push through the micro reforms that will reduce the cost of investing. But he says that these changes could take a decade to implement.

Mr Fox has now sent a long-awaited electricity-reform bill to Congress. This proposes to change the constitution to allow private generating firms to sell power directly to large consumers. The bill faces

vehement opposition from the trade unions and will spark a storm in the new session of Congress, which starts on September 2nd. If the government is to get its way, even partially, it will need to show greater acumen in deal-making than it has so far revealed.

In office for almost two years, Mr Fox can reasonably blame Mexico's recession on the outside world, while taking credit for cushioning his country from South American contagion. But from now on, Mexico's chances of leaving its southern neighbours behind will depend on its president's ability to rally political support for economic modernisation. ■

Politics in Venezuela

Poor, but fervently loyal

CARACAS

Why an inept president is still surprisingly popular

"LOVE with hunger doesn't last." So runs a Venezuelan proverb. But Hugo Chavez, the country's president, is setting out to challenge folk wisdom. Mr Chavez won the presidency in 1998—and again two years later, under a new constitution—by promising a "Bolivarian revolution". This, he vowed, would bring social justice and put an end to corruption and economic decline. Now, the economy is shrinking fast, inflation is rising, and Venezuela faces growing political violence, including a failed coup against Mr Chavez in April. Even so, he remains surprisingly popular. Most polls give him 30-35% support—down from twice that two years ago, but still more than any of his opponents or some of his South American counterparts.

What makes this odder is that the president's support is concentrated among the poor—whose numbers are rising steeply, and who are getting poorer. According to Pedro Luis España, a poverty expert at the Andres Bello Catholic University in Caracas, the number of Venezuelans unable to cover basic needs has risen by 15%, to more than 60%, in the past three years. After initially falling, the numbers in "extreme poverty" have also increased over this period. This year will see a further "spectacular" rise in poverty, Mr España predicts. Venezuela's GDP will decline by 6.3% this year, forecasts LatinSource, a New York-based consultancy. Unemployment is 15% and rising. Business organisations say 400,000 jobs were lost between January and June. Since Mr Chavez has so signally failed his core constituency, what accounts for their continued loyalty?

"Before Chavez," says an unemployed

secretary, "I had to pay 60,000 bolívares [then about \$110] in school fees for my daughter. And if you went for a medical consultation they charged you. The president came along and said health and education should be free." By abolishing fees in public schools, Mr Chavez increased enrolment by 600,000. He initially doubled the health budget, though he has since been forced into spending cuts. Vaccination programmes have expanded, while infant mortality and malnutrition began to fall (though may now rise again). "Bolivarian markets", run at first by the army and now by locals, have cut the cost of staple items to the poor. The "Bolivarian Circles", seen by the opposition as an embry-

onic popular militia, act as a kind of social service to those in need. In the countryside, the promise of land redistribution under a controversial agrarian reform law keeps hopes alive.

But given the economy's problems, none of this might count for much were it not that Mr Chavez has become the object of quasi-religious veneration. His supporters often say that he was "sent by God" and is the only hope for the poor. "Nothing and no one can touch him. He's the saviour of Latin America and part of the rest of the world," says Juancho Gonzalez, a retired radio journalist and devoted follower of the president.

Commentators from both sides of Venezuela's bitter political divide agree that Mr Chavez, who is a *mestizo* (of mixed race) of modest provincial origins, speaks a language the poor can understand. They see him as one of themselves. "He's the only president who's ever visited the slums where the opposition says only muggers live," says Angelica Gil, an unemployed housewife. "We'll continue to support him no matter what, even if we have to go hungry."

Mrs Gil was sitting at an open-air office set up by the Bolivarian Circles. Behind her hung a copy of a naive-style painting often seen at pro-Chavez rallies. It shows the president on his knees in the jail cell where he was held after staging a failed coup (when a paratroop lieutenant-colonel) against a democratic government in 1992. From the clouds above, Simon Bolívar, Venezuela's independence hero, hands him down a sword, while angels look on. In an accompanying text, the painter describes how this scene appeared to him in a dream. For richer Venezuelans, the dream is, at best, a confidence trick. Many of the poor still cling to it despite their darkening economic nightmare. ■



The masochistic cult of Saint Hugo, patron of coups

Brazil's presidential election

On the attack

SAO PAULO

The battle for the centre turns negative

HAVING slipped to a distant third place in the opinion polls, with his campaign on the brink of collapse, Jose Serra, the presidential candidate of Brazil's governing centre-right alliance in October's election, chose a risky strategy when the candidates' free daily campaign slots on television and radio began last week. He launched all-out attacks on Ciro Gomes, the populist candidate in second place. To highlight Mr Gomes's hot temper, for example, Mr Serra replayed a clip of a radio phone-in, in which Mr Gomes called a listener an "idiot". It seemed to do the trick: this week's polls show that while Luiz Inacio Lula da Silva of the left-wing Workers' Party remains well ahead, some respondents have switched from Mr Gomes to Mr Serra (see chart).

Attack ads aside, the campaign has become a stampede to the political middle ground. That is partly a reaction to recent financial turmoil—and partly because while voters may want change, they distrust extremism. In meetings with President Fernando Henrique Cardoso last week, both Mr Gomes and Mr da Silva stopped short of formally endorsing a new \$30 billion IMF loan agreement, but made reassuring noises about maintaining fiscal discipline and low inflation, as the accord requires. For his part, Mr Serra, the most pro-market candidate, promises more jobs.

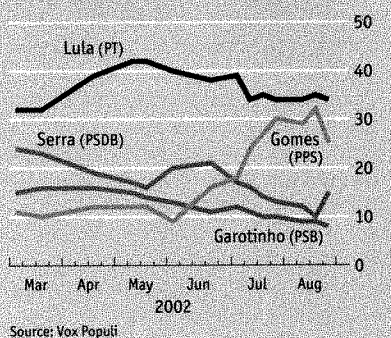
Mr da Silva, a bearded former trade-union leader, is making increasingly convincing efforts at moderation. While his opponents scrap, he stays above the fray—the candidate of "love and peace" as he puts it. This week he won the backing of Jose Sarney, a conservative former president.

By contrast, Mr Gomes looks inconsistent. Having recently said that he "couldn't care less about the markets", he then named Jose Scheinkman, a noted free-market economist, as an adviser. This, and his cosying up to some of the conservative oligarchs he claims to oppose, are causing disquiet among leaders of his soft-left Popular Socialists.

The campaign's more centrist tone, and Mr Serra's signs of life, have helped to steady financial markets. Brazil's currency, the *real*, and its bonds, have strengthened over the past fortnight. And at a meeting in New York this week, international bankers agreed not to make further cuts in their credit lines to Brazil. Meanwhile, new figures showed that Brazil's weakened currency is helping its trade balance. The government

The plot thickens

Opinion poll support for Brazil's presidential candidates, %



Source: Vox Populi

now hopes for a surplus this year of \$7 billion, up from last year's \$2.6 billion.

All of this should assuage fears of a default on Brazil's public debt. But investors remain nervous: the Central Bank was this week unable to roll over a batch of dollar-linked bonds at acceptable interest rates. The nerves may only be calmed if and when Mr Serra begins to look capable of beating not just Mr Gomes but Mr da Silva. Mr Serra, because of his broader alliance, is entitled to as much free media time as both his main rivals combined. But he still faces a challenging task. ■

The Arctic

Warming up

OTTAWA

The Inuit launch new campaigns

FOR the 150,000 Inuit who live in four countries around the Arctic rim, the warming of one of the world's coldest places is making a life of hunting seal and caribou and herding reindeer more arduous. Melting ice and permafrost restrict access to hunting grounds. Indeed, the Arctic's sensitivity to rising temperatures makes it the "canary down the mine" of climate change, says Sheila Watt-Cloutier, the newly elected president of the Inuit Circumpolar Conference (ICC).

The Inuit (also known as Eskimos) are split roughly evenly between Greenland (where they have home rule), Canada (where they control Nunavut province) and Alaska (where they are less organised), with half a dozen villages in Siberia. Every four years, Inuit leaders from all four countries meet at the ICC general assembly. At the latest, held this month in Kuujuaq in north-eastern Quebec, they decided to make promoting the Kyoto protocol on climate change their priority.

Canada has large oil and car industries,

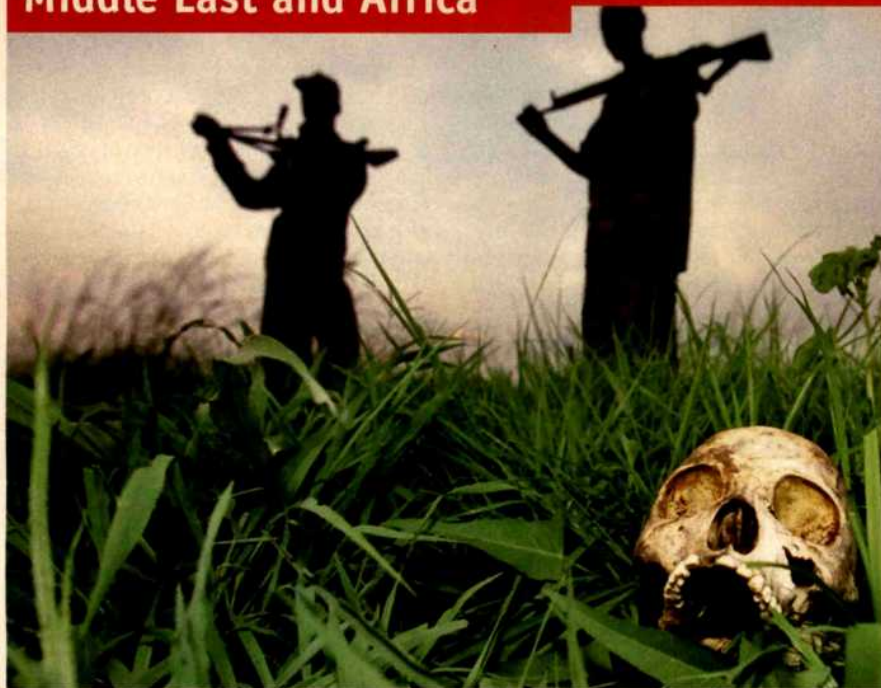
and has hitherto been sceptical about Kyoto. But opinion is now moving towards ratification, pushed in part by the Inuit. At a recent meeting of Canada's provincial premiers, Nunavut's Paul Okalik led the arguments in favour.

In Canada, the Inuit have proven clout. A group led by Ms Watt-Cloutier pushed hard for an international agreement to ban a dozen persistent organic pollutants (such as some pesticides and industrial chemicals), approved as the Stockholm Convention in May last year. Carried north by prevailing winds, these pollutants do not evaporate in the Arctic cold. They have infected the meat and berries that are staples of the Inuit diet. The milk of nursing mothers in the Arctic has been found to contain up to eight times as much of these pollutants as that of women tested in Copenhagen, Toronto or Moscow. Unusually, Canada's cabinet ratified the convention immediately after signature.

Ms Watt-Cloutier is now pushing Canada's government to assert its sovereignty over the waters of the Arctic archipelago, which the United States has never acknowledged. The Defence Ministry has yet to order the powerful ice-breaker promised in the 1980s after an American supertanker crashed uninvited through the Northwest Passage. The Liberal government cancelled as too expensive its predecessor's plans to buy nuclear submarines, so Canada has no under-ice monitoring system. Two coastal patrol craft made a brief journey this summer—no match for any lurking foreign submarines.

For all their successes, the Inuit are weakened by their dispersal between countries. Their dialect varies and they have three different scripts. The ICC's language commission wants all to adopt the Roman script. The Inuit language is disappearing in western Canada, as well as in Chukotka, in Siberia. Since news tends to stop at national boundaries, they also want to link up Inuit radio stations in Greenland and Canada. Then they might make even more noise. ■





War and peace in Sudan

A merciless battle for Sudan's oil

MAYEN JUR, SUDAN

While politicians talk peace, the fighting intensifies

AS THE battle starts, mortars, grenades and machinegun bullets rip into a column of 1,200 government troops. Clouds of white smoke and panicked birds billow and flutter. Standing under a thorn tree with Peter Gadeat, the rebel commander, your correspondent was observing a set-piece slaughter in the Sudanese savannah, another day of death in Africa's largest country, and its longest war.

The government's men advance at a rush. When they are less than 100 yards away, 3,000 rebel fighters rise up from the grass, and the serious killing begins. From 30 yards, they spray each other with sub-machineguns. They shoot wildly; unsurprisingly, since many are children. But within half an hour, the government's soldiers—black militiamen in the pay of Sudan's Arab regime—are fleeing.

The rebels' losses are light: around 30 killed and 100 badly wounded. The government's losses are much heavier, but impossible to count. Knowing they can expect no mercy, the wounded drag themselves silently into the elephant grass to die. One 15-year-old leans in a daze on a stick of bamboo, bubbles of blood bursting from his side. As he breathes, he moans involuntarily: his lungs are punctured. He cannot walk, and the nearest doctor is hundreds of miles away.

As this battle took place, in the remote

Western Upper Nile region on August 21st, Sudan's government and rebel leaders were sitting down together in Kenya for another round of peace talks. Their task is not easy. Sudan has been at war for half a century, with a pause between 1972 and 1983. The government in Khartoum is dominated by Muslim Arabs from northern Sudan. It is fundamentalist, autocratic and widely detested. The rebels of the Sudan People's Liberation Army (SPLA) are black Africans, mainly pagans and Christians, who have long craved independence from faraway Khartoum.

To inflame matters further, there is oil under Sudan, mainly in the south. The deposits are largely unexplored, but probably copious. With debts of \$17 billion, the government needs the oil. So long as the rebels control the south, it can hardly touch it. If the south were to secede, it would lose it altogether.

Despite these obstacles, astonishing progress has been made. After talks in July, the government promised southerners exemption from Islamic law and eventual self-determination. Negotiators are now trying to work out a power-sharing formula for a six-year transitional period. Both parties predict that they will soon reach a durable peace agreement.

Meanwhile, the government is trying to grab as many oilfields as it can, and the

SPLA is trying to stop them. Hence the fighting in Western Upper Nile, an oil-rich zone on the border between the north and the south, controlled by the rebels, but claimed by both sides. Its inhabitants are poor, black and non-Muslim. Because they live above oil, the government wants them out. It flattens villages of pointy grass huts with high-flying bombers, attacks civilians with helicopter gunships and sends its militias to steal their cattle and children. Once the civilians have fled, it bans aid agencies from sending food aid to the area; and then assures foreign oil firms that their concessions are beneath uninhabited land.

Last week's SPLA victory was a riposte to the latest government atrocities. On July 27th—a week after the preliminary peace agreement was reached in Kenya—government militias, backed by helicopters, routed the SPLA and drove roughly 100,000 civilians from Western Upper Nile. The fugitives tell harrowing tales. One seven-foot tribesman, who points with his spear to a septic bullet wound in his leg, says that three of his neighbours were murdered, and one of his wives stolen. A 16-year-old girl describes watching her father drown after he was chased into a river by a helicopter gunship.

By the end of 2003, oil production will have risen by 35%, according to an estimate published this week by the *Middle East Economic Survey*. Oil money enables the government to buy more high-tech weapons, and depopulate more oil areas.

But the regime has two problems. First, its actions keep it diplomatically isolated, and its links to groups such as Hamas in Palestine and Hizbullah in Lebanon (it is not linked to al-Qaeda) anger America. Second, no matter how often its men are defeated, the SPLA shows few signs of giv- ➤

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ing up. Suffering seems to toughen the southerners' resolve. "We are grateful for the mosquito nets you white people bring," says an elderly fugitive. "But what we really need are bigger guns."

Successive Arab administrations have tried to pacify the south, by promising various degrees of autonomy. But these promises have always been broken. This time, the government has offered a vice-presidency to the SPLA's leader, John Garang. But the SPLA says it needs more: military control of the south, more senior government posts, and a fixed share of the oil revenues. These measures would seriously threaten the oligarchs in Khartoum.

America has promised to apply pressure to end Sudan's war, but its policies are muddled. Many of America's more fervent Christians support the SPLA in what they see as a war against Muslim oppression. Hence America's threat to increase non-military aid to the SPLA fivefold if the government sabotages the peace talks. American oil firms, on the other hand, want their government to be friendlier with Khartoum, which is why American economic sanctions against the regime, though tougher than those imposed by others, are not as tough as America's angry Christians would like.

Blood, oil and aid

Aid complicates the picture. While European oil companies jostle for concessions in southern Sudan, their governments spend hundreds of millions of dollars trying to feed the displaced. The south's hardy pastoralists would have less stomach for the fight without the 70,000 tonnes of food the UN delivers each year. And aid keeps government troops fed, too. During their recent push into Western Upper Nile, government militiamen stole 150 tonnes of flour and vegetable oil from the UN.

In the absence of competent local pilots, the UN hires Russians to drop its food packages. The government also hires Russians, to drop bombs on the same areas. A few, it is rumoured, do both jobs.

A day with Mr Gadeat, the rebel commander in Western Upper Nile, reveals much about how the SPLA keeps its men motivated and supplied. In the morning, a light aircraft brings food for his fighters from a Norwegian aid agency, partly financed by USAID. Soon after, a UN security officer drops by, offering tips on how to shoot down helicopter gunships. In the late afternoon, a few hours before the battle, a third plane arrives from Kenya, carrying wooden crates of arms. While drilling, Mr Gadeat's men sing rousing war-songs, with refrains such as "Kill the Arabs" and "Our leader is stopping the oil".

Without greater pressure from abroad, and greater democracy at home, no Sudanese peace deal is likely to last. The government seems unlikely, unbludgeoned, to

make the necessary concessions. It has also, by barring opposition parties from the peace talks and arresting 34 dissidents this week, signalled that its dictatorship is not up for negotiation.

Meanwhile, on that battlefield in Western Upper Nile, men are dying. One militiaman, unscathed apart from two neat bullet holes through his right ankle and left shin, is eating grass to slake his thirst. He will die slowly in the sun, unless the hy-

enas get him first. He literally has no hope. Aid agencies such as the Red Cross will not help him, because the government has not allowed them into the region. The SPLA does not help enemy wounded, even if, like this militiaman, they are from the same tribe. And the only civilians in the area are those who were too feeble to flee when the government razed their villages. "They will all die," says Mr Gadeat, cheerfully. "It will only take a day or two." ■

Iraqi opposition

As diverse as Iraqi society itself

CAIRO

New optimism among the groups who oppose Saddam Hussein

BEFORE being shot in a 1958 coup, Iraq's King Faisal of Iraq regretfully described his people as malingerers prone to superstition and anarchy. Saddam Hussein's jackbooted style suggests he holds much the same opinion. Yet those alleged national traits have also helped Iraq's dictator: at least until recently they applied pretty well to the confused mass of exiled opponents who want to overthrow him.

This may perhaps be changing. The 3m

or so citizens who have fled Iraq, and the 4m who live in the autonomous Kurdish region, still support a bewildering clutter of opposition groups. But their normally drowsy offices in half a dozen Arab and European capitals now crackle with confident anticipation.

"We are talking weeks and months, not years," says Iyad Allawi, a reformed Baathist who, like many opposition veterans, has survived a quarter-century in exile ►

Uneasy allies for the duration

Ethnic and tribal	Main leaders	Based in	Comments
Patriotic Union of Kurdistan*	Jalal Talabani	Sulaymaniyah, Iraqi Kurdistan	Controls southern half of Iraqi Kurdistan
Kurdistan Democratic Party*	Massoud Barzani	Arbil, Iraqi Kurdistan	Controls northern half of Iraqi Kurdistan
Four Assyrian parties; two Turkomen parties	na	London and Iraqi Kurdistan	Represent minority language groups in northern Iraq
Alliance of Iraqi Tribes	na	na	Nineteen exiled tribal leaders out of some 150 Arab tribes in Iraq
Religious			
Supreme Council for Islamic Revolution*	Muhammad Baqer al-Hakim	Tehran	Main Shia group, active cells in Iraq. Co-operates with Iran's approval
Islamic Daawa Party	na	Damascus, Tehran, Europe	Anti-American Shia group, weakened in massacres by Saddam Hussein in 1980s
Sunni and Kurdish Islamist groups	na	na	Include small extremist factions
Nationalist			
Iraqi National Congress (INC)	Ahmad Chalabi	London, Washington	Umbrella group for pro-American opposition
Iraqi National Accord*	Iyad Allawi	London, Amman, Damascus	Ex-Baathists with good contacts inside Iraq, favours internal coup
Constitutional Monarchy Movement*	Sharif Ali Ibn al-Hussein	London	Wants Sharif Ali, heir to family that was deposed in 1958, installed as king
Two communist parties; pro-Syrian Baathists; others	na	na	Reject co-operation with America
Military			
Iraqi National Coalition	Tawfiq al-Yasiri	London	Small group of former officers, organised London conference of military exiles
Free Officers Movement*	Najib al-Salhi	Washington	Led by a former commander in the Republican Guard, who fled in 1995
Iraqi Officers Movement	Fawzi al-Shamari	Washington	Competes for American attention
1,500 exiled officers	Wafiq al-Samarrai Nizar al-Khazraji	Damascus, various European capitals	Includes high-ranking defectors, some with blood on their hands

Source: The Economist

*Member of INC

► and at least one assassination attempt.

Pressure comes from the Bush administration and its call for "regime change". Partly, this takes the form of warlike words, such as those voiced this week by Dick Cheney, the vice-president, in a speech calling for pre-emptive action. But military pressure is also increasing with advance deployments of American weapons in the region, and more air patrols over north and south Iraq. And tighter American sanctions, plus a pricing regime for Iraqi oil exports that turns away buyers, throttle Iraq's enfeebled economy.

Cranking up the engine

America has also turned its energy to recharging the Iraqi opposition, both financially and in terms of morale. The efforts have yet to produce a united front, though last month the administration invited six leading groups, including Kurds, nationalists and even an Iranian-backed Shia opposition front, for talks that were described by all as fruitful.

The details of action were not discussed, say some who attended, but the Iraqis were impressed with America's commitment to a free, united and democratic Iraq, while the Americans were pleased by promises of greater co-ordination between the groups, who have often been vicious rivals. In exchange for more American money, the opposition groups promised to crank up propaganda and recruitment efforts inside Iraq, and to do their bit to try to reassure Iraq's doubting neighbours that American action would somehow be good for them, too.

America has also reached out for new allies among Iraqi exiles, inviting jurists to map out a legal transition, and summoning tribal leaders who, it is hoped, could call on clansmen to subvert the Baghdad regime. The spirit of co-operation among the wider opposition has even inspired some former officers in the Iraqi army, an especially divisive lot, to meet in London and issue a Covenant of Honour calling for a pluralist and demilitarised Iraq. All these groups plan to hold a larger meeting soon, which, or so it is hoped, will be a sort of *loya jirga* to endorse America's role in regime change, and perhaps to draw up a plan for Iraq's future.

According to a range of opposition leaders, the mix of American pressure and higher-profile opposition activity is already causing strains inside the country. The scale and quality of defections are growing, they say, with several dozen mid-ranking officers and one major-general in the security forces having crossed over in the past month alone.

Opposition leaders differ, however, on what this all means. Mr Allawi believes that cracks in the regime are widening so fast that only small-scale American military action may be necessary for it to

crumble. Hamed al-Bayati, a spokesman for the Supreme Council for the Islamic Revolution, a Shia group, thinks Mr Hussein cannot be toppled unless America "goes for the head of the snake" by taking Baghdad. A popular uprising will be possible, he says, only if America cripples the Iraqi ruler's ability to communicate with his commanders.

For all its sudden enthusiasm, the Iraqi opposition has a long way to go before any of its parts, or even the whole, becomes an effective force. America and its allies have backed many of these groups since the 1991 Gulf war, but their fractiousness, combined with discord inside American administrations, has made for rocky relations. Some groups—the Communists, some Baathists and some Islamists—bitterly blame America for the severe distress caused by sanctions. Others charge America with serial betrayal—of a 1975 Kurdish revolt, of the 1991 uprisings among the

Shias and Kurds, of two coup attempts in the mid-1990s that were scuppered by CIA mishandling, and of hundreds of opposition activists executed when the Iraqi army captured their bases in 1996.

Yet, for all its bad memories, shady past and current feebleness, the opposition does have something important to offer. The diversity of its factions better represents Iraq's subtle ethnic and religious mix than Mr Hussein's monolithic Arab nationalism. If its leaders can overcome the bad blood between them, the opposition is not a poor model for a pluralist society.

"We're not seeking an Islamic state," says a Shia leader. "We just want to be another quietly prosperous Gulf country." "I don't care if it's a monarchy, a republic or whatever," says a Kurd who thinks Scotland is a good model for Kurdistan in an Iraqi federation. "I just want the repression to end." But see the next story for what Kurds inside Kurdistan may be planning. ■

Iraqi Kurdistan

With their eyes on Kirkuk

ZAWITA, NORTHERN IRAQ

The Kurds talk of federation and plan for independence

ONE says sort-of no, the other sort-of yes. The no comes from Massoud Barzani, leader of the Kurdish Democratic Party (KDP), who runs the north-west of Kurdish-controlled northern Iraq. Mr Barzani fears that an American war on Saddam Hussein could have dire results for the Kurds, resulting in the loss of the huge gains they have made since the creation of their autonomous enclave in 1991.

The yes comes from Mr Barzani's rival, Jalal Talabani, whose Patriotic Union of Kurdistan (PUK) controls the south-east. On a recent trip to Washington he announced that the Americans would be welcome to use his territory as the base for an attack. He then both retracted and repeated the offer.

In fact, whatever they say, the Kurds will have little choice. Once an attack was started, it would be virtually impossible for them to stay on the sidelines, especially if, as they believe, the Iraqi army collapsed, and uprisings occurred across Iraq.

There is another reason why the Kurds will probably join battle. It hangs in every government and party office in the enclave: the Kurds' official map of Iraqi Kurdistan. The map covers almost double the territory that the Kurds control today. And bang in the middle of the land they want is Kirkuk, an oil-rich city now well within Baghdad's control. The Iraqis (much like the Sudanese in the first story in this sec-



tion) will fight to the death for oil.

Officially, the Kurds are committed to a federal Iraq. But, if this came about, where would the federal borders lie, and who would draw them? The Iraqi Arab opposition groups have signalled to the Kurds that they do not believe that there is any need to sort this problem out now. Kurdish officials are inclined to agree—since they know that their Arab colleagues would never agree to their maximalist demands.

But this means that if the Iraqi regime were to collapse, the Kurds, who have up to 100,000 fighters, would hope to seize as much land as possible, as quickly as possible. They would then be able to negotiate future borders from a position of strength.

For Kurdish leaders, federation is a means to an end. The end they look to ►►

eventually is independence and, in the even more distant future, the unification of all the Kurdish lands in Iraq, Syria, Iran and Turkey. So it is all-important for them to set and get the borders they want.

But the Kurdish lands that are now controlled by Mr Hussein have been heavily Arabised. Kurds have been progressively cleansed, especially from Kirkuk, and Arab settlers have been brought in to replace them. Even so, the Kurds are confident. They do not expect property conflicts: the Arabs, they say, will flee before them.

The up-beat mood is expressed by Frey-doun Abdul Kheder, the interior minister in PUK territory. He says he knows that "Saddam is finished" because, in the past few months, Iraqi military officers have been plying him with valuable intelligence. They are doing this, he says, because they want to claim that they had always worked against Mr Hussein.

And, despite Mr Barzani's reservations, at Zawita, in the KDP's zone, mountain-



Training to be a regular

guerrillas are being trained to become soldiers in a regular standing army. As they drill, they shout: "Kurdistan or death!" A standing army for a federal unit seems a bit ambitious. But not if the Kurdish leaders are thinking forward, well into the future that all Kurds long for. ■

Israel

Cutting out the cancer

JERUSALEM

How Israel's army commander sees the Palestinian threat

THE latest broadside in the Israeli-Palestinian conflict was delivered by Lieutenant-General Moshe Yaalon, a former intelligence chief who took over as Israel's chief of staff in July. The Palestinian threat, the general told a convention of rabbis last weekend, was like a cancer, visceral and life-threatening. The *intifada* was not a popular uprising against Israeli occupation, but a premeditated war. It was in-

tended, he said, to bring about the collapse of Israeli society, and the eventual eradication of the Jewish state.

General Yaalon's words were excoriated by Israel's peace camp as an unwarranted trespass into politics. On the right, they were celebrated. He then elaborated his view of the world in an interview with *Haaretz* published on August 29th. "[The Palestinians] believe that time is on their

side and that, with a combination of terrorism and demography, they will wear us down." Faced with this threat to its survival, Israel's only option was to secure "victory", which the general defined as "the very deep internalisation by the Palestinians that terrorism and violence will not defeat us... If that is not seared into Palestinian and Arab consciousness, there will be no end to their demands of us."

For General Yaalon, the practical conclusions were clear. There must be no unilateral concessions and no withdrawals that could be interpreted as signs of weakness, as the Israeli withdrawal from Lebanon in 2000 had been widely interpreted. As for the security fence that the government is building along sections of the Israeli-West Bank border, the general said that if it were up to him, he would "spend the money better elsewhere".

He said he spoke as "a humanist, a liberal, democrat and a seeker of peace and security". Other Israeli seekers of peace see themselves thrice wounded by the general's tirades.

Many of them have focused their frustration on the personality of Yasser Arafat. But General Yaalon's condemnation took in all the Palestinian leaders. Like the Nazis in Germany after the second world war, he said, they must all be barred from serving in a reformed Palestinian administration. Nor did he allow any room for diplomatic mistakes during the peace negotiations: he himself, he said, had always doubted the sincerity of the Palestinian side. Above all, the general repudiated the late Yitzhak Rabin's view that the Palestinians, even at their most violently rejectionist, do not constitute a threat to Israel's existence.

Implicit in the chief of staff's statements was a distinct lack of enthusiasm for the tenuous "Gaza, Bethlehem first" agreement concluded last week by his putative boss, Binyamin Ben-Eliezer, the defence minister. Mr Ben-Eliezer, who is also the leader of the Labour Party, says that he is pleased with the way the agreement is working in Bethlehem. But the army has let it be known that it wants to postpone the next planned withdrawal, from the West Bank town of Hebron, until after the Jewish holy days in the autumn. And Ariel Sharon, who is plainly in tune with the thinking of his army commander, this week pooh-poohed the whole deal as "just moving a couple of jeeps".

There was a crumb of comfort for depressed Israeli peaceniks in some bold talk by the British chief rabbi, Jonathan Sacks. Interviewed in the *Guardian* on August 27th, Mr Sacks confessed that "there are things that happen on a daily basis [in Israel] which make me feel very uncomfortable as a Jew." He had always believed, he said, that Israel "must give back all the land for the sake of peace." But then, how many divisions has the chief rabbi? ■



Yaalon tells the rabbis of the Palestinian danger



Germany's election

It's not over yet

BERLIN

With three weeks to go, Gerhard Schröder (above) has pulled back lost ground

NEVER have German voters appeared so undecided or so volatile, so close to an election. In early May, Chancellor Gerhard Schröder's Social Democrats were trailing some ten percentage points behind the conservative opposition in the opinion polls. By June, they had narrowed the gap to just a couple of points. Early this month, they were once again a good 6 or 8 points adrift. Now, according to some pollsters, they have edged back to within a single point of the conservative Christian Democrats. However, with only three weeks to go before the election, an unusually large proportion of voters—one in three—has yet to decide what to do.

The floods in the east of the country, the worst for more than a century, have helped lift the Social Democrats' sagging fortunes. Mr Schröder's decisive handling of the crisis contrasted with the bumbling reaction of his conservative rival, Edmund Stoiber. The chancellor's decision to put off for a year the next stage of planned income-tax cuts, due to take effect on January 1st, and to impose a one-off levy on corporate profits to raise funds for the flood victims, may be economically questionable, but it looked better than Mr Stoiber's panicky zig-zag. First the conservative leader supported extra corporate taxes,

then he condemned them. His eventual solution—in effect, an increase in new debt as a means of providing flood relief—risks pushing Germany's already awkwardly high public deficit over the European Union's 3% limit.

The Social Democrats watched jubilantly as their ratings rose. But they know that their fortunes could well sink again as the flood waters retreat. The focus of attention is already shifting after a much-hyped televised debate on August 25th.

Such an American-style show-down had never been tried before in democratic Germany, where the parties, not their bosses, are supposed to play the leading role in election campaigns. Despite the excitement—some 15m Germans tuned in—the outcome was disappointing. The hoped-for cut and thrust turned instead into an awkward double interview, with each contender talking through a moderator. An ever-grinning Mr Stoiber was deemed to have performed well by his own rather wooden and gaffe-prone standards. Mr Schröder, more of a media star, showed none of his usual punch or wit.

Mr Stoiber scored higher on the economy and jobs. Mr Schröder came over as the more likeable of the two and likely to make the better chancellor. Both men

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Charlemagne returns next week

stuck to vague promises of more jobs, less public spending, lower taxes and a stronger economy; both wanted greater social justice and a revamped social welfare system. Neither man spelled out how he would achieve this. No wonder so many voters are undecided. According to pollsters, most Germans do not think much of the present government. But they do not believe Mr Stoiber's lot would do better.

Mr Schröder's greatest weakness remains the economy. Figures published last week showed that GDP had grown by 0.3% in the second quarter, the same as in the previous quarter, after shrinking in the last three quarters of 2001. But consumer spending remains almost flat, while unemployment continues to climb. Figures for August, due out next week, are expected to show that the total number out of work has risen for the first time above the level that Mr Schröder inherited when he swept to power four years ago on a solemn pledge to cut the dole queues. If he did not achieve that goal, he said, later defined as no more than 3.5m without a job, he would not deserve to be re-elected.

Mr Stoiber, who as premier of Bavaria runs one of Germany's most affluent states, will not let him forget that. But his own record is not exemplary. Unemployment in Bavaria is the second lowest in Germany (not the lowest, as he claims): 5.7% compared with a west German average of 7.9%. But it has jumped by a fifth over the past year, three times the national rise. Last year, Bavaria's economy grew by a meagre 0.9%. Yet that was still better than the 0.6% for Germany as a whole, and that is what counts with voters.

Mr Schröder will now be doing his ►►

► damndest to deflect attention from the economy. Recent talk about a possible war against Iraq could help him. He has said Germany should take no part in military "adventures". Mr Stoiber, usually keen to show solidarity with America, has been slower to criticise the Bush administration's war plans. Most Germans strongly oppose to any American-led military intervention in Iraq. This issue could also help boost the chances of the ex-communist, and pacifist, Democratic Socialists. If they fail to win the 5% required to get into parliament, Germany's complex voting system would almost certainly ensure a parliamentary majority for Mr Stoiber's conservatives. If the ex-communists do get back in, the Social Democrats still have a chance. Mr Schröder must be praying for America's sabre-rattling to continue. ■

The Balkans

Thankless tasks

PRISTINA

Cracking down on crime in Kosovo

ARENT the killing fields of the Balkans supposed to be settling down and living happily ever after, with less and less need for international supervision or aid? That is what many western politicians—and their voters—have been hoping.

Sadly, things still feel far from settled in the wilder bits of Kosovo—where over 60 people, including 11 police officers and three NATO soldiers, were hurt in a recent scuffle between peacekeepers and local Albanians. In nearby Macedonia, where war between Slavs and Albanians (some

Kosovo-based) was averted last year, the risk of fresh conflict still exists.

All in all, this summer has been one of the tougher, and more thankless, periods for the international overlords of Kosovo, whose predecessors were showered with roses by grateful Albanians when they arrived, on the heels of a defeated Yugoslav army, three years ago. It is a sign of the times that Michael Steiner, the (impeccably liberal) German who runs Kosovo for the UN, has been depicted in the local media with a Hitler-like moustache.

But this souring of relations between Kosovo's protectors and parts of the ethnic-Albanian community is not all bad news. Both Mr Steiner and General Marcel Valentin, the French commander of NATO's mission, have taken what they knew to be a calculated risk by vowing to crack down harder on crime, racketeering and contraband among the Albanians—as well as imposing their authority on recalcitrant Serbs in the north of Kosovo.

As part of this drive to enforce the law, some senior veterans of the Kosovo Liberation Army, the guerrilla force which helped oust the Serbs from the province in 1999, have been arrested on charges of illegally detaining, torturing and killing fellow Albanians. Earlier this month Ramush Haradinaj, a warrior-politician and senior member of the province's ruling coalition, was indicted for his alleged role in a shoot-out in western Kosovo.

For the increasingly effective UN police force, these arrests are only the beginning of an overdue effort to rein in Kosovo's notorious underworld, in which dealers in prostitutes, heroin, cigarettes and guns have made vast fortunes. Some Kosovar Albanians—especially supporters of Ibrahim Rugova, the moderate who holds the province's (relatively powerless) presidency—will undoubtedly breathe a sigh of

relief if the foreigners' bid to root out crime and extortion succeeds. But in the short term, more noise will be made by backers of the hard-line warlords who now find themselves in the UN's sights; and opinion in the province is certainly divided.

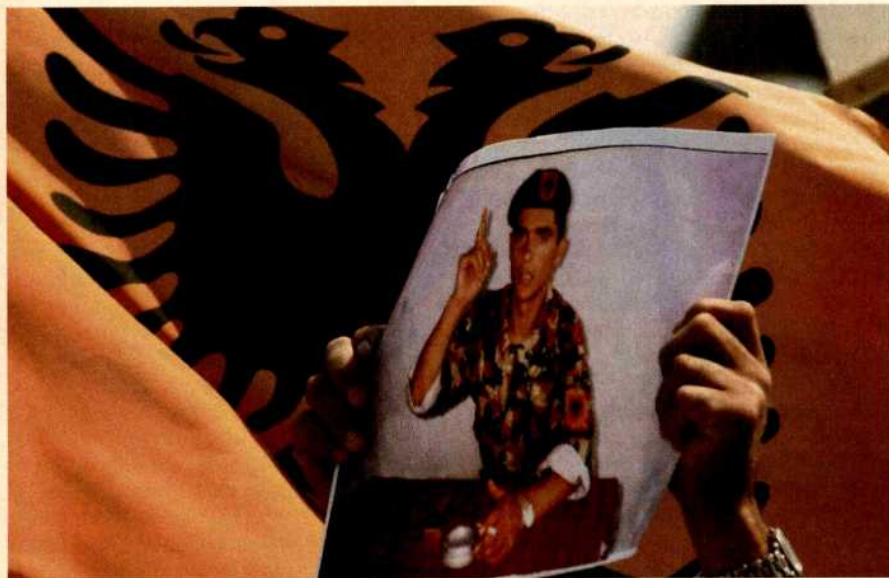
In any case, despite the anti-UN slogans on the streets, Kosovo's administrators are quietly confident of vindication. They acknowledge that self-described war veterans have staged anti-UN protests in all Kosovo's towns over the past three weeks. But only one of these rallies—in the Haradinaj clan's west Kosovo heartland—has turned violent, and then only mildly so; lives were never in danger. One international policeman argues that most Kosovars are tired of living in a province where criminals wield huge power; that feeling, he reckons, will prevail over orchestrated xenophobia. Nor have the demonstrations made any real impact on the lethargic way of life of rural Kosovo, which is now largely peaceful. Inter-communal killings have almost stopped—albeit partly thanks to self-segregation by rival ethnic groups.

The UN says routine crime is almost under control, though organised crime is not. In some places, Serbs and Albanians even mix openly. Black-garbed Serb pensioners can shop in the market in the Albanian-dominated town of Gnjilane without the American armoured vehicles which have hitherto been needed to protect them.

The UN's new toughness towards Albanian extremism has also had a beneficial effect in Macedonia. The arrest in Kosovo, earlier this month, of six alleged members of the so-called Ilirida Republican Army, a new Albanian-nationalist group, produced sighs of relief in Skopje, where Slav-Macedonians often accuse the West of coddling armed Albanians.

In the latest sign of tension in Macedonia, two policemen were shot dead this week outside the Albanian-dominated town of Gostivar. Under the hard-line leadership of Ljube Boskovski, Macedonia's interior ministry would almost certainly relish the excuse to settle scores with local Albanians, armed and otherwise. So the need to keep Macedonia's broiling tensions under control at all costs—if possible by apprehending Albanians bent on destabilising that country, while they are still in Kosovo—is keenly felt by all western diplomats and soldiers in the region.

Looking a little further ahead, these outsiders see grounds for cautious optimism. As long as Macedonia's election next month can proceed in peace, and local elections in Kosovo a month later are relatively smooth, it should be possible to start reducing the NATO mission, to below 30,000 from the current 35,000. Britain, in particular, wants to halve its contribution from over 2,000 to less than 1,000, as military challenges in other parts of the world—such as Iraq—loom larger. ■



For some, they are all still heroes

Spain and its Basques

Silencing the secessionists

MADRID

A ban on Batasuna will not be the end of the terror story

BANNING Batasuna, the political wing of the violent Basque separatist group ETA, is, according to Spain's prime minister, Jose Maria Aznar, the only option left in his battle to stamp out terrorism. But the ban has stirred up a hornets' nest.

Batasuna has enjoyed all the benefits of democracy, including official funding received by Spain's political parties, while giving tacit support to ETA, which continues to kill and intimidate—836 people have died so far. According to police reports, links between the two are so strong that no real distinction can be drawn. After 25 years of a democratic system, including a strong dose of devolution for the Basque country, the government in Madrid thinks it is time to stop feeling guilty for Spain's past under Franco and to get tough on those who undermine freedom.

Mr Aznar has a parliamentary majority behind him for his assault on Batasuna, and most Spaniards back him. At a special session of parliament, recalled from recess on August 26th, members passed a motion asking the government to outlaw the party. The full process could take several months but Spain's campaigning magistrate, Baltasar Garzon, has already moved to suspend its activities. A separate bid to ban it by the attorney-general is also under way. Judge Garzon has frozen Batasuna's bank accounts and forbidden its leaders to organise demonstrations. On August 27th, the Basque regional police began to implement a legal order to shut down Batasuna offices throughout the Basque country. Electricity and water companies have been ordered to cut off supplies.

Just a few hours after the parliamentarians voted, ETA placed a bomb near the courts in the Basque town of Tolosa. Police carried out a controlled explosion. Batasuna's leader, Arnaldo Otegi, dragged out of party headquarters in Bilbao, described the ban as typical of the "repressive" Spanish state. But he saved his worst spleen for the mainstream Basque Nationalist Party, which controls the regional government and police, calling it a "traitor". "If you want war; you'll get it. The armed struggle is the only way," shouted Batasuna supporters gathered outside the building.

What now? Batasuna could contest the moves, even though that means recognising the Spanish courts. But initially its leaders have been keen to present themselves as victims of the Spanish state. Some party officials have announced they will move



Batasuna is all stirred up

their headquarters to Bayonne in the French Basque country.

Relations between all of Spain's political parties have been strained. The Basque nationalists who voted against the ban have been accused of "cowardice" by members of Mr Aznar's People's Party. So, too, the Catalan Nationalists and United-Left coalition, who abstained. The opposition Socialists supported the move but writhe in discomfort at the aggressive tone of Mr Aznar's followers. Basques, meanwhile, fear that the run-up to municipal elections in May (where Batasuna has traditionally done best) will be bloody. ■

Turkey

A man for all Turks?

ANKARA

How Kemal Dervis could change the face of Turkish politics

HE'S finally made up his mind. After keeping the nation guessing for the better part of a month, Turkey's former economy minister, Kemal Dervis, has declared that he will be going into politics after all. He has thrown in his lot with the Republican People's Party, known as CHP, Turkey's oldest left-wing party. The announcement marks a dramatic shift in Turkey's politics, with parliamentary elections due on November 3rd.

Mr Dervis's personal popularity is such that, until last week, he was being wooed by one political party after another. For secular-minded urbanites, he is the only effective answer to Recep Tayyip Erdogan, Istanbul's former mayor, who continues to be labelled an Islamist, though he insists he does not believe in mixing religion with politics.

For the country's industrialists and for western governments, Mr Dervis is the

only person capable of steering Turkey out of its financial mess. Since being called home from the World Bank 18 months ago, he has made notable progress, pushing through a programme of fiscal and economic reform that won for Turkey a huge rescue package from the International Monetary Fund and the Bank. But much remains to be done. Mr Dervis insists that unless "there is full co-ordination between the ministries dealing with economic matters"—by that he probably means, unless he is at the helm of the economy (he is not interested in becoming the next prime minister)—Turkey could plunge back into the abyss once more.

With Mr Dervis at his side, the electoral fortunes of Deniz Baykal, the bristly CHP leader, seem much improved, to the detriment of a clutch of leftist parties, notably that recently formed by Ismail Cem, the former foreign minister, whom Mr Dervis had initially supported. Mr Dervis pulled back after Mr Cem brusquely turned down Mr Baykal's invitation to join forces under the CHP banner. Uniting the left is Mr Dervis's most cherished goal.

Can he and Mr Baykal snatch victory from the hugely popular Mr Erdogan? The race will be tight, but with 20 or so parties in the running, the most likely outcome is another coalition government. Mr Dervis makes no secret of his wish to work with Mr Cem as a possible coalition partner. But Mr Cem first has to muster the minimum 10% of the vote needed to win seats in parliament. Without Mr Dervis on his team, that will be tough.

Some of Mr Dervis's friends, including a prominent liberal economist, Asaf Savas Akat, have suggested that the CHP share power with Mr Erdogan. Mr Erdogan has certainly gone out of his way to assuage fears over his alleged Islamist agenda. He says he wants Turkey to join the European Union. He also says he will not field female candidates wearing the Islamic style headscarf; Virtue, the Islamic-leaning party from which Mr Erdogan broke away last year to form his Justice and Development Party, did so and was banned. Joining hands with a party that is clearly supported by a significant number of Turks, if not its meddlesome generals, would surely help shore up Turkey's wobbly democracy, the argument goes.

There is still a chance that Mr Erdogan will be prevented from running. He stands charged with subverting Turkey's secular system during his stint as mayor. A verdict is expected on September 17th. But if Mr Erdogan is excluded, his party could draw sympathy votes.

The outcome many Turks fear is one where Mr Erdogan's followers, discouraged, join forces with ultra-nationalists opposed to Europe and the IMF. Then Mr Dervis's dream of a prosperous, European-oriented Turkey would come to nought. ■

Romania's poor

Easy to preach, harder to do

BUCHAREST

Free markets have the cure for poverty, maybe, but politicians have voters

THE bankers at an investment conference tried to sound bullish. One day, they said, Romania might catch up with the European Union. New technologies are taking hold. Some factories in Bucharest and in Transylvania, the western province, look as sleek as German ones. Use of credit cards, mobile phones and the Internet is rising fast. The economy should grow respectably this year. Inflation may dip below the target of 22%. Many outsiders see Adrian Nastase's proclaimedly free-market government as Romania's most promising since it discovered democracy.

Alas, that is not saying much. A standard view in Brussels is that, while other Central Europeans should join the EU in 2004 or 2005, Romania will have to wait until 2012 at the earliest. Corruption and poor infrastructure, made worse by recent floods, hold it back. The courts and roads alike are rotten. A third of all Romanians live in poverty. The rural poor can subsist on what they grow. The urban poor have a tougher time of it.

Take Gara de Nord, a working-class Bucharest district one metro stop from the prime minister's office. At first glance, it appears to be moving up in the world. The railway station at its heart has been cleared of beggars and prostitutes. A French hotel chain, Ibis, has done up a once squalid property nearby. A Daewoo car dealership, an Orange mobile phone shop and a 24-hour McDonald's now mark out the neighbourhood's corners. Even street dogs, which used to roam in packs, now move about furtively in ones and twos. But grinding poverty has not gone away.

Ioana Breaza, 57, and her four-year-old niece live in one room across the road from the McDonald's. They share her courtyard's single open latrine with 20 others. The state gives her \$22 a month for disability and child care, not enough to get a large lump in her breast examined or to send her niece to kindergarten.

Gianina Radu, 37, lives around the corner, in a broken-down, rat-infested tenement. Her two rooms are dingy but neat, the walls adorned with cheap icons of her favourite saints. Her husband earns \$70 a month as a foreman of a flower stall. She gets another \$18 in state benefits. They have four children, the oldest aged 20, the youngest four. Gas, electricity and water cost all her husband's salary in the winter and half of it in summer.

That is, if the Radus paid. They don't:

Scandinavian shoppers

Have car-boot, will travel

STROMSTAD, SWEDEN

Some prices are lower across the border. So that's where they go

SYSTEMBOLAGET, Sweden's state-owned alcohol retail monopoly, is doing a roaring trade this summer at its outlet in Stromstad, a small coastal resort just south of the Norwegian border. From the queue outside, stretching down the street and around the block, you could think that the Swedes are an exceptionally thirsty bunch. No: these are Norwegians using their strong krone to fill their car boots with bargains priced in Sweden's krona.

For example, a bottle of decent Australian barbecue wine costs SKr69 (\$7.40), as against NKr92 (\$12) in Norway. Norwegians can save nearly 40% on a typical trolley-load of groceries, 50% or more on tomatoes or butter, 60% on chicken and other meat products. Furniture, especially sofas and kitchen units from Ikea, is another draw.

The price differences are due partly to Norway's high tariffs on imported foods and huge taxes on alcohol and tobacco, and partly to a sharp rise in its krone, now—thanks to continuing international confidence in Norway's oil-fuelled economy—at its highest ever against the Swedish krona. Cross-border shopping in the Stromstad region is reckoned to have surged by 30% in the first half of this year to NKr1.3 billion.

Yet Swedes too can go bargain-hunting—in Copenhagen, where booze is cheaper and variety wider. In return, Danes, with a krone of their own (both countries belong to the European Union, but neither uses the euro), are increasingly taking the Oresund bridge-and-tunnel into Sweden to buy low-taxed children's shoes and clothing. They can also make worthwhile savings on books, do-it-yourself items and even spectacles. For cheap drink, they drive south into



Germany; Carlsberg, a Copenhagen-based brewer, says one-fifth of the beer drunk in Denmark arrives this way.

Political responses have varied. Norway's agriculture minister, Lars Sponheim, tried to shame his compatriots into shopping at home by snootily disparaging them as *Harries*, the kind of folk who wear track-suits and spend their holidays in caravans. The *Harries* sensibly put two fingers up, and opposition politicians are now calling for lower taxes at home instead. Danish politicians are doing likewise.

Though many retailers across the region, perhaps surprisingly, spy benefits in price transparency, the cross-border shopping boom, also maybe surprisingly, has not set off a public chorus for euro membership. Opinion polls put pro-euro sentiment in Sweden and Denmark fairly stable at around 60%. But analysts say support for the euro is due more to its successful launch than hopes of lower prices. And Norwegians remain stubbornly hostile even to joining the EU, let alone the euro.

like many poorer Romanians, they wait to be cut off. Mrs Radu is glad to see the new businesses in the district, but thinks they are "just for the rich". Constantin Alexandrescu, who runs a scissor- and knife-sharpening shop in front of Mrs Radu's tenement, is more hopeful. He charges 40 cents to repair scissors, 30 cents to sharpen knives. That is a lot for locals, he admits, "but then everyone needs a sharp knife." He reckons to make \$110 a month, enough for his wife and two children to get by on. "But not enough for a Big Mac," he grins, waving his oil-stained hands.

Can Mr Nastase, a former Communist turned social democrat, do more for the

poor? His government has raised the minimum wage to about \$50 a month and has promised to put up pensions. But it has no spare cash to improve health care or education for the poor. Barely a fifth of Romanians pay income tax. Plans to increase revenue by lowering taxes but getting them paid will take time. On the spending side, cut more jobs in state companies—in the oil industry, notably—urge the IMF and World Bank. But in the short run, that means more people out of work, and Mr Nastase is not a banker or a development economist, but an elected politician. His government, balking at the social cost, thinks it has done enough already. ■



Transport finance

Getting there faster

Why not make those who benefit pay for transport improvements?

AS LONDON booms, gridlock beckons. Average speeds on the most congested routes are now down to 3mph. In the past 15 years, the capital's population has grown by 600,000, nearly 10%. With the population forecast to grow even faster, congestion is likely to get worse, not helped by a queue of transport projects stalled for lack of funding.

Top of the list is the £10 billion (\$15 billion) Crossrail high-speed link between Docklands and Heathrow via a tunnel between Paddington and Liverpool Street stations. If you add other much-needed improvements, such as the East London line, the extension to the Docklands railway and light rail schemes in West London, the total amount of money required is probably nearer £20 billion.

It is not only London which faces the threat of creeping paralysis. The Strategic Rail Authority has a long list of projects for which it has no funding, notably a new high-speed dedicated express route to the north from London, costing between £15 billion and £20 billion.

Where are these huge sums to be found? The chancellor, Gordon Brown, shows little enthusiasm for financing transport projects—especially those in London. The Treasury, jaundiced by the cost overruns on the £3.5 billion Jubilee line in the 1990s, believes that the capital is over-indulged compared with the rest of Britain. Crossrail, whose benefits according to its promoters are double its costs,

does not even feature in the government's ten-year transport plan.

Significantly, however, the chancellor is warming to the idea that another way may have to be found to finance transport infrastructure. A recent local government green paper backs the idea that councils should be allowed to share in development gains, by raising business rates in special areas. It is not a big step from this to using the tax system to capture the value of transport developments.

In theory, the idea of taxing increases in land values makes eminent sense. Why should developers, landlords and tenants make untaxed windfall gains from transport improvements funded by general taxation? The Jubilee line is a case in point. After a good deal of arm-twisting, the owners of Canary Wharf put up £180m, a fraction of the amount it gained as a result of the line. Other developers and landlords along the route paid nothing, although the value of their properties soared by as much as four times.

Don Riley, a south London property developer, claims that the Jubilee line could have been financed without any government subsidy if part of the increase in land values had been captured. The £5.5 billion Channel Tunnel Rail Link has similarly led to a boom in land values in areas such as Kings Cross, Ebbsfleet and Stratford. A new high-speed line to the north would bring big gains to any city along its route. When public money brings windfalls to a few,

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Bagehot is on holiday

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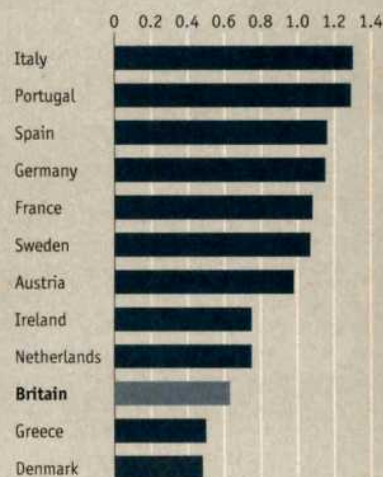
why should the state not take a share?

The idea of taxing increases in the price of land may sound dangerously radical but actually it is not. It has a history stretching back to the mists of fiscal time. It is advocated passionately by some academic economists but politicians have been unenthusiastic, not least because of problems of implementation. The Treasury's reassessment of land value taxes in the green paper is thus encouraging, though officials stress the review is at a very early stage.

Current methods of capturing planning gains are opaque. Section 106 of the 1990 Town and Country Planning Act empowers local authorities to reach agreements with developers. This has enabled some of the gains that result from planning approval to be tapped on behalf of local communities. But the results are ad hoc, uncertain and often bear little relation to

Short changed

Transport investment as % of GDP, 1996



Source: Commission for Integrated Transport, 2001

► the potential returns.

Other countries have adopted a more coherent approach. In America, \$10 billion has been raised in the last five years by anticipating increases in property tax revenues. Tax increment financing (TIF) captures increases in property values resulting from development. San Jose in California, one of the fastest-growing cities in the country, has raised \$1.4 billion in this way to redevelop its city-centre.

In Britain, several ways have been proposed to capture part of the increases in value due to planning and infrastructure gains. Stephen Glaister of Imperial College and Tony Travers of the London School of Economics have proposed an infrastructure fund for London financed by a hypothecated levy on the national non-domestic rate, adding perhaps 6% to business

rate bills. CB Hillier Parker, a commercial property agent, suggests that Crossrail could be financed by a levy of 2p per pound on the rates, or perhaps a 2% freehold levy on businesses thought likely to benefit from the new line.

Ken Livingstone, the mayor of London, is seeking to persuade the government that this is the right way to tackle the burden of financing transport. But if local authorities are to be allowed to borrow against future tax revenues, the chancellor will have to relax his iron grip on local government spending. With 96.5% of all taxes paid to the Treasury, the scope for local initiative is currently non-existent. It is perhaps not a coincidence that Britain's highly centralised economy has led to decades of under-investment and one of the worst transport systems in Europe. ■

Tourism

Cute

The Japanese are flocking to Britain, thanks to Becks and Beatrix

BEATRIX POTTER and David Beckham are unlikely bedfellows, you might have thought. But what these two very different icons of English style have in common is the power to lure thousands of Japanese tourists to Britain.

In the months since the World Cup, the number of Japanese booking holidays to Britain has tripled, according to the Japan Travel Bureau. Recognising the England captain's hysteria-inducing appeal in Japan, the travel bureau is now offering special "Beckham Tours". These coach trips take in Leytonstone, east London, where Mr Beckham was born; his school in Chingford; his homes in Essex and Cheshire; and Old Trafford, where his club, Manchester United, is based. The travel bureau's target of 1,500 bookings to Britain in the 12 months to March 2003 has already been exceeded: the current figure is upwards of 2,400.

This year also marks the 100th anniversary of that masterpiece of children's literature, "The Tale of Peter Rabbit". The Japanese have always been fans of the various Potter books, and the Lake District, where she lived for much of her life, has become the second most popular destination for Japanese tourists, after London. Around a quarter of the 80,000 or so who visit Hill Top, Potter's farm near Sawrey, are Japanese. Richard Foster, manager of the World of Beatrix Potter and chairman of the Lake District Japan Forum, says that this summer's visitor numbers are about 25% higher than expected.

Whence Japan's fascination with a mischievous bunny and his furry



Football fever

friends? The standard explanation, says Mr Foster, is that, since many Japanese have learnt English through the Peter Rabbit books, the appeal is sentimental. More important, he believes, is the particular brand of Englishness that the books retail. The wonderful illustrations, classily reproduced on Wedgwood breakfast bowls and teacups, Mr Foster adds, also have a quality, much admired by the Japanese, of being *kawaii* (pronounced kah-why-ee), or "cute".

Which brings us back to Mr Beckham. On the face of it, the chisel-jawed, designer-outfitted athlete has little in common with the quaint imaginings of a homely farmer. But *kawaii* might also be the very quality the Japanese respond to in Mr Beckham—and cuteness of a peculiarly Potteresque kind at that. Just look at his World Cup-period hairdo: a straight steal from the pages of Beatrix Potter, surely, combining the two-toned contrast of Tommy Brock and the spiky quiff of Mrs Tiggy-Winkle.

Gambling

Coming up trumps

Thanks to the repeal of the betting tax, the gambling business is booming

BRITAIN'S service sector has suffered along with its metal-bashers from the slowdown in the economy. Yet one service industry, the world's second-oldest—gambling—is experiencing a renaissance.

A decade ago, high street betting shops were sullen, dodgy places. Regulations required curtains to shield pedestrians from the evil business inside. Carpets were forbidden, lest punters got too comfortable. Food and drink, even the soft variety, were prohibited. Britons, it seemed, were content to tolerate gambling, but not to love it.

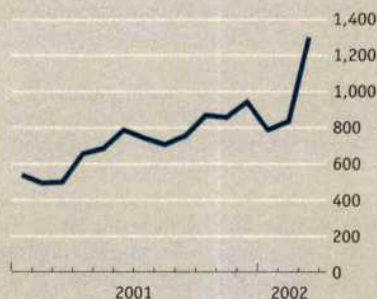
Then came three important changes. In the 1990s, the National Lottery brought gambling in from the cold, letting the middle classes experience the thrill of a flutter. Secondly, the Internet found that gambling was, like pornography, perfectly suited to the medium. That led, thirdly, to Gordon Brown's decision to eliminate betting tax.

In a recent paper, three academics, David Paton and Donald Siegel of the Nottingham Business School, and Leighton Vaughan Williams, director of the Betting Research Unit of the Nottingham Trent University, show how the repeal of the tax is helping to usher in a new "golden age" for gambling. Since October, when taxes on the value of bets were eliminated and replaced by one based on bookies' profits, turnover from racing and sports bets has risen by 70% to £1.3 billion (\$1.97 billion) a month, or 1.6% of Britain's GDP.

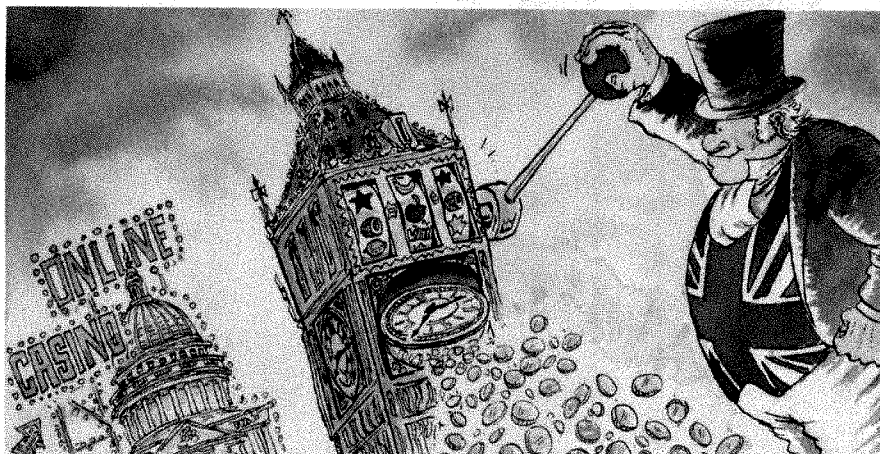
The tax change, say the authors, reflects the government's desire to maintain Britain's share of the global gambling industry. It was also spurred by tax competition from Ireland. Though the tax cut will reduce receipts in the short term, retaining the old betting tax would have been far ►►

Double top

British gambling turnover, £m



Source: HM Customs & Excise



► worse as bets were fleeing offshore. As part of the tax cut, Internet bookmakers agreed to return home from places like Antigua. Today, although the dotcom boom is but a memory, bookmakers are one of the online world's few success stories.

The tax cut was just the first step in a wider liberalisation of betting. Although a new Gaming Act is not expected before next year, Richard Caborn, the sports minister, last month laid out some of its measures. These include allowing food in betting shops, letting casino punters sip cocktails at the baccarat tables and relaxing the prize limits for old dears enjoying a spot of bingo. Coming soon may be a move to allow the use of banknotes in fruit machines, giving punters an easier way to pursue a particularly addictive style of gambling, which worries Britain's anti-gambling activists. Will London become Las Vegas East?

Britain already has some of the most liberal gaming laws in the world. While most other rich countries chose to make betting on horse-racing a state monopoly, Britain legalised private bookies in the 1960s. In America, tax and regulations were conceived with an eye towards mitigating the social costs of gambling, rather than fostering competition. There, religious groups, which view gambling as a sin, and Indian tribes, which get rich from largely un-taxed casinos on reservation lands, hold sway.

That is a loss for the Americans, since gambling is becoming a big export business for Britain. In this summer's World Cup, around a third of the industry's turnover came from foreign punters placing bets with British bookies, with much of this coming from rich Asian football fans. Other bets come from America, where puritanical laws—driven by fears of corruption and thrown games—ban sports bets everywhere except in Nevada.

The tax cut has spurred innovation. Person-to-person betting, offered by the likes of www.betfair.com, gives punters a chance to cut out the middleman, making for better odds than the bookmakers'.

Though greater competition puts pressure on bookies' profit margins, the increase in turnover wrought by the tax cut is more than compensating. Indeed, despite the stockmarket's dismal days this summer, William Hill's initial share offering was one of its few successes, raising £950m. Other bookies look set to follow.

At a time when the European Union is still pressing Britain for tax harmonisation, gambling is a rare reminder of the benefits of tax competition. Will the lesson stick when it comes to taxes on income and property? Don't bet on it. ■

The euro

Sleeping giant

The euro is less liked, and less talked about, than was expected

OPTIMISTS like to think that hostility to something alien—such as foreigners, or their currencies—declines on closer acquaintance. Thus scepticism about the single currency was supposed to soften once Britons realised that euros wouldn't stain their palms or spontaneously combust.

That optimism seems to have been misplaced. A poll by YouGov—for KPMG and the *Sunday Times*—which quizzed holiday-makers before and after their summer breaks, suggests that paying for sangria with actual euros had little or no impact on people's views. Other pollsters also report a general hardening of opinion against ditching the pound (see chart). Complaints across the euro area about opportunistic price hikes may be part of the explanation.

In so far as Britons are thinking about the single currency, most remain unimpressed. However, the euro is not being thought or talked about much at all. Monetary union has never excited ordinary voters as much as the small bands of fanatics who either love or loathe it. Now, though,

polls also suggest, the proportion of people who consider it an important issue is at a low ebb. But since both the government and the Tories—who are in enough of a pickle without reviving their euro civil war—are keeping *shut* about it, the euro's low profile is not all that surprising.

Of course, high politics tend to drop down news agendas during the summer. Still, this year was supposed to be different. The government is due to reveal whether Britain (and the euro) have passed Gordon Brown's five economic tests for euro entry by next June. Many observers predicted that a referendum on entry would be called for next spring, which would require prior legislation. But nothing much seems to be happening.

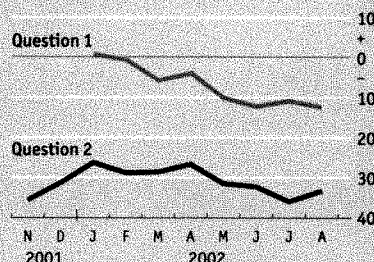
One interpretation of this silence is that Tony Blair has shied away, at least for this parliament. Another is that the euro remains one of the issues upon which the prime minister thinks his reputation will hang, and upon which he is ready to make a stand. On this analysis, the government's silence on the euro does not betoken doubt about its poll-winning prowess, but is rather a sensible strategy designed to avoid unduly antagonising the voters.

Political observers, trying to choose between these two views, will have noted a little tour made this week by Jack Straw, the foreign secretary, to the Celtic fringe. Mr Straw was talking of the need for a European constitution, and not about the euro; but he may also have been trying to goad the Tories into saying silly things about the European Union as a whole so that, when the real hostilities commence, they can be portrayed as extremists. The forthcoming Labour Party conference (possibly) and the results of the five tests next year (certainly) should clear things up. By then war with Iraq may have intervened, but even that, Mr Straw insisted this week, would not be enough to deflect the holding of a euro referendum. ■

Breeding contempt

Q1: If the government said that the UK had passed the five economic tests for membership of the single currency, and recommended that we should join, would you accept this recommendation and vote to join the euro in a referendum?*

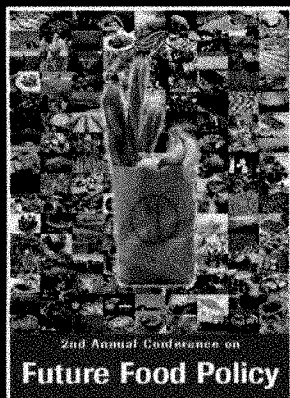
Q2: If a referendum on the single European currency were held today, would you vote for or against replacing the pound with the euro?*



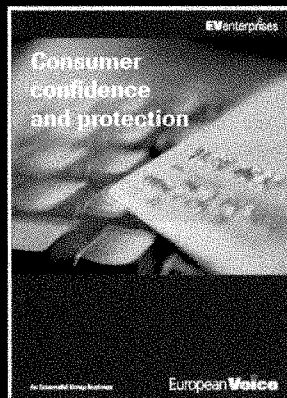
* Balance of those in favour minus those against
Source: Barclays Capital

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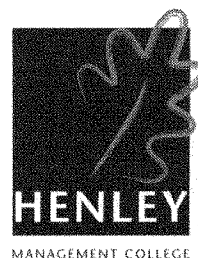
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Nestlé

A dedicated enemy of fashion

VEVEY

Most companies claim to run their business for the long term. Nestlé is one of the few that really does

PETER BRABECK is used to the name-calling by now. Boring, lame duck, sleeping giant—he has heard them all. Sitting in his office in Vevey, overlooking Lake Geneva, the chief executive of the world's biggest food company is almost proud that Nestlé has been dismissed as dull for much of its 136-year history. What worries him far more are accusations that the Swiss group is swapping a consistent, long-term strategy of controlled expansion for an unbridled acquisition spree to pep up its growth rate—and that it is doing so just when dullness is back in fashion in the business world.

By any definition, Nestlé is already a giant. It owns an array of global brands, including Nescafé, the world's bestselling instant coffee, Perrier and Vittel water, KitKat chocolate and Friskies pet food. It towers over its rivals, with a market capitalisation of \$86 billion, more than \$50 billion of annual sales and pre-tax profits forecast at \$5.5 billion for 2002.

The company is keen to grow even bigger, and acquisitions have a role to play. Between 1985 and 2000, Nestlé spent some \$26 billion purchasing other companies. By contrast, in the past 18 months alone it has splashed out more than \$18 billion. It is now considering a bid for both Adams, which makes chewing gum and sweets and is valued at around \$5 billion, and Hershey Foods, America's leading

chocolate company, worth some \$12 billion. While most of its previous 250 or so takeovers were small, Nestlé has acquired a taste for big, expensive bites, such as the \$10.3 billion purchase last year of Ralston Purina, a pet-food maker, and this August's \$2.6 billion takeover of ChefAmerica, a frozen-snack producer. Wolfgang Reichenberger, Nestlé's finance chief, has even said the company would sacrifice its cherished AAA credit rating for the right deal.

For Mr Brabeck, there is no contradiction here—and certainly no change in strategy. As he points out, acquisitions have always been part of the Nestlé way, with bouts of feeding usually followed by periods of digestion. Indeed, its purchase of Carnation in 1985 was the biggest-ever takeover outside the oil industry at the time.

Nor does Mr Brabeck see anything wrong with a streak of opportunism, even at a high price, when a "filet mignon" comes up for sale. "They are very rare, those pieces," he says. "When you have such an opportunity, it fits strategically and you want to be a leader in that area, I don't see why you shouldn't act." By this definition, Ralston Purina was pure *filet mignon*—as, he concedes without bitterness, was Bestfoods, which was snapped up by Unilever, his nearest rival. He describes Hershey, perhaps a little disingenuously, as "*entrecôte*"—a slightly inferior

Also in this section

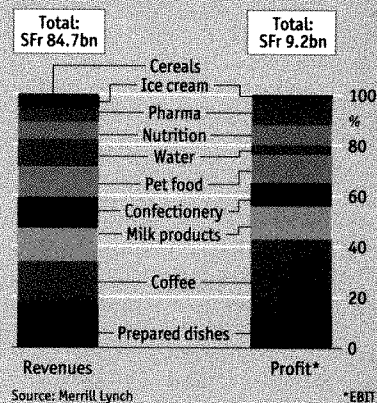
- 44 Hershey Foods for sale?
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cut of meat. After all, with a 43% share of American confectionery sales, it would give Nestlé a big lead in the world's biggest chocolate market, where the Swiss group is currently number three.

If Nestlé does decide to pounce, it will be relatively well-placed to deal with Hershey's quirks and the misgivings of the local community (see next story). Nestlé has a reputation for managing smooth integrations, even of difficult companies, because it tends to let the target's management run the merged division, rather than insisting on its own people taking over. Putting Ralston Purina's management in charge of the group's global pet-food business and basing it in Ralston's home town of St Louis has worked well: the division is exceeding its targets for both cost and revenue synergies. "We want a company because it has successful management. Why should I destroy what I have paid for? If we decided to buy, I wouldn't have any problem making an integration work at Hershey," declares ►►

Sumptuous spread

Nestlé estimated results, by division, 2001



► Mr Brabeck.

Indeed, he finds the reaction to his brand of pragmatism a little frustrating. He points out that the same analysts who today criticise Nestlé for thinking of buying big rivals were only two years ago asking what it was going to do with its piles of cash. "Nestlé's long-term view is perhaps more coherent than the view of some of the analysts," he suggests.

Deal doubts

The more serious charge, levelled by those same analysts, is that Nestlé is only stepping up its pace of acquisitions because its organic growth is running out of steam. Certainly, the group is likely to miss its 4% target for sales-volume growth this year. In the first six months, growth slipped to 3.5%, from 4.6% in the same period last year.

Nor does Nestlé compensate for its more sedate growth with sparkling profitability. Although its operating margin is at last rising again, increasing to a decent 11.7% this year, that is not much different from the 11.1% at smaller Danone, and it is well shy of Unilever's reported 15%—though Unilever, unlike Nestlé, strips out restructuring costs.

But this assessment of Nestlé's financial performance ignores two things. The first is that Mr Brabeck has been reducing the group's reliance on highly profitable but mature businesses, such as coffee—the profit margin for Nescafé is around 40%—by moving quickly into faster-growing areas that require initial heavy investment, such as pet food, water and ice cream. Over the past three years, he has turned Nestlé into the world leader in the first two. In ice cream, the company is now vying with Unilever for the top spot, following the purchases of Ice Cream Partners (Haagen Dazs), Schoellers in Germany and Dreyers in America.

This activity has depressed profit margins. As a result, Mr Brabeck is now concentrating on improving efficiency. His first cost-cutting programme, which involved the closure or sale of 114 factories, has saved more than \$2.5 billion since 1997, well ahead of expectations. Nestlé is now rolling out three programmes to increase efficiency at second-tier factories, cut administration costs and harness group-wide economies of scale in purchasing and research. Total savings should exceed \$3.5 billion over the next four years.

John McMillin, an analyst at Prudential Securities, expects around 70% of these savings to be ploughed back into advertising and promotions, rather than feeding straight through to the bottom line. This reinvestment is typical of Nestlé: under both Mr Brabeck and his predecessor (and mentor), Helmut Maucher, the company has eschewed short-termism, preferring to think ahead in decades. "Shareholder value is for me nothing but a paradigm that

says focus equals efficiency and that complexity is inefficiency," says Mr Brabeck. "The problem is that when you carry this paradigm out over a longer period, you are basically starting to kill your own business. You run out of growth."

Nestlé, by contrast, embraces complexity. It has factories in 84 countries, 260,000 employees and 6,000 brands, give or take a few. Mr Brabeck claims that the skills his company has developed as it has expanded are hard to replicate and are thus a real business advantage. But it is an advantage that makes a difference only over the long term. In the short term, having a local presence in so many countries, refusing to cut its long tail of smaller brands (as Unilever is doing), and properly managing both, is not cheap. Nestlé's hugely complicated matrix structure of product and regional responsibilities creates costs. "Ap-

plying global management principles to one of the most decentralised businesses in the world is a colossal management challenge," says Nic Sochovsky, an analyst at Merrill Lynch.

Although that makes Nestlé a difficult "story" to sell to investors, Mr Brabeck is not perturbed by such considerations. To him, what counts is success on the ground. In South Korea and China, Nestlé lost money for a decade; today, both countries are highly profitable. While competitors pulled out of Russia during the 1998 currency crisis, Nestlé stuck it out and doubled its market share in chocolate, coffee and ice cream over the following 18 months, achieving market leadership in all three areas. The company's long-term view of the bottom line may be somewhat unfashionable, but it has also been rather successful. ■

Hershey Foods

Bitter times for a sweet town

HERSHEY, PENNSYLVANIA

Fear and loathing in America's chocolate town

MILTON HERSHEY must be turning in his grave. The company he built into America's biggest chocolate maker, with such goeey offerings as Hershey's Kisses and Reese's Peanut Butter Cups, is trying to put itself up for sale. Ironically, it is the Hershey Trust, to which Milton handed his 77% voting stake in Hershey Foods in 1918 after the death of his wife, Kitty, that now seems determined to deliver his life's work

into the hands of a competitor—perhaps even a foreign one.

The trust, though, is not really to blame. Its job is to finance a school for disadvantaged students set up by the childless Milton and Kitty, both devout Mennonites, and to safeguard an endowment that, at \$5.4 billion, is now one of the richest educational institutions in America. Granted, that is a lot of money and explains why the students—who had to milk cows by hand until 1989—have a full-sized football stadium, marbled halls and chauffeurs to ferry them to class. But the trust wants to expand the number of students from 1,200 to 1,500, and it has a clear fiduciary duty to diversify its portfolio. The stake in Hershey is its only investment.

The trouble is that Hershey is not a normal company. Hershey the business and Hershey the town (in Pennsylvania) are intricately intertwined. The self-styled "sweetest place on earth" features streets such as Chocolate Avenue and Cocoa Avenue, and street lights shaped like the firm's Kisses. Milton Hershey designed everything in the town, from its parks to the sewerage systems, to improve his workers' lives. Today, Hershey employs half the town's 12,000 residents. Many managers, including a former chief executive, are graduates of the trust's school.

Hence the community's outrage at a possible change of ownership. Pennsylvania's attorney-general, Mike Fisher, is capitalising on local ire and taking the trust to ►►



A crying shame, for some

► court. Monty Stover, a 102-year-old former executive who knew Milton Hershey personally, is typical in his disdain for the planned sale: "Mr Hershey would never have considered this proposition. He would have said: 'Gentlemen, you are wasting your time and mine. Goodbye.'"

This means that Hershey will be tricky to integrate for any of its suitors, believed to include Nestlé, Philip Morris's Kraft subsidiary and Cadbury-Schweppes. Kraft may have the edge, not only in being American, but also because Hershey's current boss, Rick Lenny, used to be a senior executive at Nabisco, which Kraft swallowed in 2000. But then again, Nestlé already has a commercial relationship with Hershey, which distributes its KitKat bar in America. And the Swiss group has already weathered a similar "hostile" takeover: in 1988, it bought Rowntree, a British confectionery maker with strong links to its home town of York.

In the end, the resistance of the people of Hershey may not be enough to stop their company being snatched from under their noses. After all, if the taste of Hershey's chocolate—which, legend has it, is made with sour milk—is not enough to put off the bidders, what is? ■

German airlines

Welcome to the cheap seats

FRANKFURT

The battle to offer Germans cut-price flights is warming up

GERMANS are getting used to offers of cheap flights. Ryanair, an Irish no-frills airline, will fly you from Hahn, 100km (60 miles) outside Frankfurt, to Stansted, north of London, for €9.99 (\$9.82). Deutsche BA, a subsidiary of British Airways, is offering flights within Germany from €34, although around €100 is more typical. And this week, Lufthansa, the national flag carrier, declared that it was "making flying within Germany better value than ever".

From the end of October, Lufthansa will sell some seats on flights within Germany for as little as €88 each way. In November, some 200,000 seats, or up to 10% of its domestic capacity, will be on offer at the lowest fares. Lufthansa also plans to cut fares to and from Britain and Turkey, and later other European destinations.

Until now, Lufthansa has treated low-cost competition with disdain. Even now, it says that it is not tackling the upstarts head-on—its new prices are still way above those of true budget airlines. On the domestic front, in particular, it sees little need to defend itself against the small fry. The



Another low-cost traveller

new fares, says the airline, have less to do with fighting low-cost carriers than with filling empty seats, mainly on off-peak flights. Lufthansa's prime targets are people who travel by car or train. By offering these marginal passengers cheaper fares, it hopes to increase the proportion of seats occupied on domestic flights, now 62-65%, by about five percentage points.

That said, Lufthansa does face some direct, low-cost competition on routes between big cities at home, as well as on international routes. Across Europe, fares are under pressure, thanks to the weakness of the world economy as well as the challenge from new airlines. Lufthansa is the third big European carrier, after British Airways and the Netherlands' KLM, to cut fares within a couple of months.

Yet Lufthansa's main response to the low-cost operators is not fare cuts, but a no-frills carrier of its own. It has consistently said that it will not start a low-cost airline under its own banner, for fear of cannibalising its own traffic and damaging its brand. However, Eurowings, a German regional airline of which Lufthansa owns 24.9%, has said it will launch a low-cost carrier, called germanwings (sic), in October. Lufthansa has an option to increase its stake in Eurowings to 49%.

The German low-cost market is even starting to look crowded. EasyJet, a British no-frills carrier, has an option to buy Deutsche BA. Ryanair is expanding its operations at Hahn. Virgin Express is due to start flights from Cologne-Bonn airport in December. And TUI, a big travel group known until a few months ago as Preussag, and Germania, which already flies cheaply from Berlin to Cologne-Bonn and Frankfurt, announced this week that they are joining forces to launch a new low-cost airline. There will not be room for everybody to make money. There should, though, be more bargains on the way. ■

Pharmaceuticals

Trouble in the making

Sloppy manufacturing comes under fire, but inefficiency is the real problem

FOR all the glamour of invention, the latest blockbuster medicine, like the hottest new fashion, can unravel if manufacturing falters. Witness the slew of drug makers that have fallen foul of the Food and Drug Administration (FDA), their regulator in America, over how they make their pills and potions. Hardest hit, so far, is Schering-Plough, which has been taken to task for failing to meet FDA standards at four plants. In May, the company signed a decree promising to do better and paid a \$500m settlement to the agency. Eli Lilly, Abbott and Wyeth are among other firms to have drawn frowns from the FDA.

Some of these firms' woes come from turning out products containing too little medicine or too much contamination. This alarms consumer groups, such as Public Citizen, which worry about the FDA's ability to police manufacturing given its meagre manpower and funding. Last year, the agency performed only about a third as many inspections as it carried out in 1980.

But headline-grabbing lapses in quality are the exception rather than the rule, says G.K. Raju, executive director of the Pharmaceutical Manufacturing Initiative at the Massachusetts Institute of Technology (MIT). A far wider problem is inefficiency in the manufacturing process.

Although early research and development (R&D) is usually seen as the hard part of producing a drug, manufacturing is not easy either. For chemical-based drugs, simply producing the active ingredient can take a dozen chemical reactions, followed by formulation and packaging. Before they can market their medicine, drug makers have to register their manufacturing process with the FDA, which checks that it is turning out uniformly safe and effective doses and that the company has systems in place to sample product batches for quality.

At this point, however, innovation slows down dramatically, according to Mr Raju. Since companies are in a rush to get their products to market, they tend to take their laboratory-scale methods and expand them to industrial proportions, rather than think of new ways to make pills on a much bigger scale.

Moreover, much as companies boast about their prowess in R&D, manufacturing is saddled with old equipment and techniques. Few drug firms have top manufacturing people on their executive boards. According to Charles Cooney, also ►



Never mind the quality

at MIT, so long as companies see manufacturing simply as a matter of compliance with regulatory requirements, rather than an opportunity to cut costs and production time, change will be slow in coming.

There are lessons to be learned from other industries, according to Doug Dean of PricewaterhouseCoopers. The chemicals industry, for example, keeps its production lines running in continuous processes that are more automated and efficient than the batch methods used by drug makers. Genzyme, an American biotech firm, has copied this approach to get more out of its production sites. Mr Dean wishes that drug makers would look even further afield, to the semiconductor and aviation industries, which do better on turnaround times and process uniformity.

The FDA is doing its bit to promote change. On August 21st, it announced plans to revamp the way that it oversees drug manufacturing. It intends to give priority to those products and processes that pose the greatest risk to public health, to root out inconsistencies in regulation, and to promote new manufacturing technologies among pharmaceutical executives and its own inspectors.

Mr Raju hopes that companies will see that innovating makes economic sense. At the moment, manufacturing consumes 25% of the average drug company's revenues, and it takes up to six months to get a product through manufacturing and on to pharmacy shelves. Mr Raju reckons that more efficient manufacturing could translate into \$500m of savings over the lifetime of a \$1 billion-a-year blockbuster drug. As big pharmaceutical firms come under increasing pressure from patent expiries and weak drug pipelines, such savings are sure to grow more appealing. ■

Russian electricity

In need of shock therapy

To avoid a full-blown power crisis, Russia must reform its sprawling, crumbling electricity industry

STRONG, sober and presiding over a growing economy, Vladimir Putin has every chance of being re-elected as Russia's president in just under two years' time. But if he wants to be remembered as the leader who laid the foundations for future economic growth, Mr Putin must tackle the reform of Russia's long-neglected power industry—and quickly.

Artificially low electricity prices have been one of the main forces driving Russia's recent economic expansion. The government sets the rates, and has powerful motives for keeping things as they are. It wants to make sure that Russian households remain lit, and that firms stay afloat. This is nice for the Russian people but less so for United Energy Systems (UES), the world's biggest electricity group in terms of installed capacity. Captive to the government, which owns a majority stake, cash-strapped UES has watched its equipment crumble. If present trends continue, Russia will soon face an electricity crisis.

This autumn, Russia's Duma (parliament) will debate a bill to reform UES, which owns the national grid and controls about 80% of Russia's generating capacity. The bill lays the groundwork for breaking up UES and liberalising the electricity market in order to attract investment and usher in competition in generation.

Electricity is a political issue the world over, but especially so in Russia, still in the midst of post-communist transition. The debate over reform pits the central government against regional governors. Although Moscow controls wholesale electricity tariffs, the governors control retail

prices. They are adamant about keeping this power so they can protect industries to which they have ties. Moreover, they are determined to maintain low electricity prices for households, which pay about \$2 a month to keep their lights on, roughly the price of a cheap bottle of vodka.

This cannot last. If the industry is to attract investment, wholesale electricity prices need to double by 2005, according to UES. Philip Vorobyov of Cambridge Energy Research Associates estimates that the power industry needs between \$20 billion and \$50 billion in investment over the next ten years. Eighty gigawatts, almost half of Russia's generation capacity, must be retired over the next 20 years as it reaches the end of its productive life, while 120 gigawatts needs to be added, more than the total installed capacity of France. If there is no surge in investment, Russia will suffer from nationwide electricity shortages some time between 2003 and 2008. Many regions have already been stuck without power.

The government has already taken steps to avoid this dark fate. Mikhail Kasyanov, the prime minister, issued a decree on electricity reform in July 2001. This created the grid company and system administrator as legal entities within UES. The next step is to cobble together hundreds of disparate generators to create ten giant wholesalers that would account for 45% of Russia's generation capacity. Then the government will break up the vertically integrated regional power companies. Up to 15% of generation capacity will be sold on the open market by 2005, according to the ▶▶



Electricity is cheap, but not always available

plan. Sergei Dubinin, deputy chief executive of UES and a former head of the central bank, wants to sell stakes in two or three wholesalers to western utilities.

One crucial question is the fate of electricity prices. Originally, the plan envisaged a politically independent federal commission that would regulate both retail and wholesale tariffs. Not surprisingly, though, politics has dominated price regulation. With the 2004 presidential poll nearing, the pace of tariff increases has started to slacken. The government plans to raise prices by just 11% in 2003 in dollar-adjusted terms after a 32% leap in 2001.

Now comes the hard bit

With the Duma due to debate the power bill as early as September, things will get even trickier. On August 30th, a committee of lawmakers and government officials was to meet to issue amendments to the bill. Analysts expect the committee to refuse to allow the federal government to set retail prices—and the government is expected to cave in over this issue. However, the government should be able to get the Duma to go along with breaking up and reorganising regional electricity companies, says Fyodor Tregubenko of Brunswick UBS Warburg. That would be a blow to the regional governors, as it would create larger regional companies too big to remain under their thumb.

Conscious of the stakes involved, foreign investors are starting to throw their weight around as well. They own one-third of UES shares and have not forgotten how, two years ago, Anatoly Chubais, head of UES, tried to sell generators on the cheap to well-connected local tycoons. According to David Herne, portfolio manager at Brunswick Capital Management and a UES board member, relations between the management and minority investors have since improved, but problems persist.

Earlier this month, for instance, investors were shocked to discover that UES had signed what they contend was an unfavourable contract with Renaissance Capital, which has control over more than 25% of Kuzbassenergo, a large UES subsidiary. The agreement makes it easy for Renaissance to gain the generation capacity of Kuzbassenergo cheaply in a future tender. Unfortunately for UES shareholders, other financial investors are positioning themselves for similar deals.

Despite the problems, foreign utilities are starting to sniff out opportunities. After all, Russian electricity rates are forecast to rise faster than those in Western Europe. Foreign firms also want to export power to Western Europe, provided they can secure long-term contracts. E.ON, Germany's largest utility, has agreed to draw up new investment projects jointly with UES. Other companies that have shown interest include Electricité de France, AES of the Un-

ited States and Italy's Enel.

Even before the Duma passes the reform bill, UES is seeking out new investment. It will hold an auction later this year for a stake of around 25% in a power plant near St Petersburg. This would be the first tender in the industry aimed at foreign strategic investors. Meanwhile, Yukos, a Russian oil company, is positioning itself to buy generating capacity, and thus ensure control of its electricity supplies.

Ultimately, the reform bill's chances of creating a liberalised, investment-friendly electricity market will depend largely on Mr Putin himself, since parties allied with

the Kremlin hold the majority of votes in the Duma. The real test, however, will be in the implementation. Mr Vorobyov questions whether Mr Putin will turn the federal commission that sets wholesale prices into a truly independent body, empowered to set tariffs that reflect true costs.

Doing this would have an electric effect on UES's share price and encourage foreign utilities to buy into generation capacity. But Mr Putin may yet prove unwilling to bear the political costs of reform: higher inflation, lower growth in the short term and social disquiet. If so, Russia's crippling power shortages will only get worse. ■

Public relations in China

Puffing away

HONG KONG

A nation of 1.3 billion waiting to be spun

THE public-relations industry arrived in China in 1993, reckons Li Hong, the local boss of Fleishman-Hillard, the world's second-largest PR agency. That was the year when commercial advertising in print media was liberalised. It was also a time when memories of the Tiananmen Square massacre had begun to fade—enough, at least, for bosses of foreign multinationals to resume kowtowing in Beijing. Hardly a week went by without a new joint venture or product launch that needed professional hype.

Since then, China has been perhaps the fastest-growing PR market in the world. PR revenues worldwide fell by 3% last year; but they rose by 33% in China, to \$242m. That makes China the second-largest market in Asia after Japan (which is still about twice as big). Not only is there a boom in local agencies—China now has 10,000 PR people, according to a trade association—but every big international agency is investing. In June, Ogilvy, part of WPP, a marketing giant, bought H-Line, a leading local agency, to become the largest PR firm in China.

Multinationals investing in China still account for most of the demand for PR services, and China's entry into the World Trade Organisation helps. Not only are more foreigners hoping to familiarise Chinese consumers with their brands, from Nokias to BMWs, and hiring PR people to get them mentioned in the local press. They are also using PR firms for their "deep localisation", says Matthew Anderson, Ogilvy's president in Asia. This includes advice on how to communicate with employees and even on finding talent.

The biggest development, however, is soaring demand for PR among Chinese companies. For much of China's (mostly state-owned) corporate sector, PR re-



mains an outlandish concept. Increasingly, however, Chinese firms are courting foreign capital. Companies such as AsiaInfo, a provider of Internet infrastructure that was the first Chinese company to list on America's Nasdaq stockmarket, happily pay for hand-holding from international PR firms for their first contacts with investors.

Others, such as Haier, the leading Chinese white-goods maker, have international ambitions for their brands and are hiring PR firms to seek out consumers. Others still, such as the thousands of textile factories that are springing up as rich-country import quotas fade out, hire agencies to reach western clothes retailers. And some of China's private-sector firms become clients hoping to be introduced to influential party cadres: quite a few PR people, including Mr Li, are former government officials. Small wonder that Fleishman-Hillard reckons its present customer breakdown—20% Chinese and 80% multinational—will reverse in a matter of years.

Face value Logan's run

Can Don Logan repeat at AOL what he did for Time Inc?



OF ALL the management changes that have shaken AOL Time Warner in recent months, none captures the shift in the balance of power within the troubled media giant better than the recent elevation of Don Logan. This time a year ago, Mr Logan presided over a demoralised Time Inc publishing empire, whose staff feared that their distinctive editorial culture was being trampled on by the eager young upstarts from AOL, led by Bob Pittman, to whom Mr Logan reported. A year on, Mr Pittman has been ejected from the group, and Mr Logan has been promoted to run one of its two new umbrella divisions under Richard Parsons, the chief executive. His responsibilities include cable, magazines, book publishing and interactive video. But his biggest headache will be sorting out all those former antagonists at the struggling AOL.

There is a delicious irony in this appointment. For one thing, Mr Logan has long been sceptical about the transforming power of the Internet, and has never minced his words on the subject. In 1995, when asked about Pathfinder, then Time Inc's web effort, he replied: "It's given new meaning to me of the scientific term black hole." Mr Logan must now oversee the attempt to extract AOL from its own black hole: its earnings before interest, taxation, depreciation and amortisation dropped by 27% year-on-year in the second quarter. The SEC is investigating accounting practices at the division.

Mr Logan and many of his Time Inc colleagues were especially resistant to the early brash attempts by AOL types to treat magazines as just another marketing tool, and the company as a relic in need of a shake-up. Although the 79-year-old Time Inc's titles have themselves embraced the world of celebrity and show business—Tom Cruise, "Spider-Man" and "Star Wars" have each graced recent *Time* covers—a sense of superior editorial mission still lingers in the Time-Life building. This

fierce independence collided with the aggressive efforts by AOL to turn publishing into a cross-promotional vehicle. Now, it is 58-year-old Mr Logan's turn to give the orders to the young Turks at AOL.

Yet, incongruous as this burly, plain-talking publishing boss may seem at the high-tech AOL campus in Dulles, Virginia, Mr Logan's appointment could turn out to have been inspired. The task at AOL—a close-knit culture marked by complacency—is similar to that which greeted him when he joined Time Inc in 1992, as chief operating officer. Then, the publishing group was a bureaucratic, rather snobbish place, beset by infighting.

Mr Logan, a no-nonsense southerner, had no time for that. He set about turning Time Inc into a more meritocratic, less political organisation, with a more decentralised structure. Not that the group has entirely shed its sense of privilege or creature comfort. But Mr Logan has taken harsh decisions, including cut-backs and firings, when necessary.

As businesses too, AOL and Time Inc have more in common than meets the eye. Each relies on a mix of subscription and advertising revenues. Like some magazine titles, AOL needs to reverse slowing subscriber growth, and to fight aggressive efforts by its competitors, notably Microsoft's MSN, to Hoover up its customers.

A head for numbers

Capturing subscribers is one of Mr Logan's specialities. In the 1970s and 1980s, he worked at Southern Progress, a publisher in Alabama with such titles as *Progressive Farmer* and *Southern Living*, rising to become its boss in 1986. A one-time mathematician and computer programmer at NASA, he is at home mining customer data for marketing ideas. "He instantly spots the relationship between numbers," says a former colleague.

There are other parallels, too. When Mr Logan turned up in New York, fresh from Alabama, observers said there was no more growth to be had from magazines; profits at Time Inc were shrinking. Yet he went on to preside over 41 consecutive quarters of year-on-year profits growth. In the first half of 2002, Time Inc increased its share of the American magazine market by 1.4 percentage points to 24.9%, its highest first-half share since 1989. Mr Logan's hallmark was "brand extension": *Time* begat *Time for Kids*, *People* begat *Teen People*, *People en Espanol* and

In Style, and so on. Thanks to spin-off launches and acquisitions, under his command the number of Time Inc titles grew from around 20 to 140.

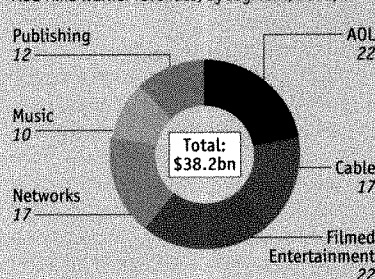
It would be foolish to underestimate the job that Mr Logan and Jonathan Miller, AOL's new boss, have taken on. The company needs stability, yet the pair have already begun to conduct purges. AOL also needs to secure wider cable access. To this end, and under an agreement concluded last week, AOL Time Warner will buy AT&T Comcast's 27.6% stake in Time Warner Entertainment, a mix of cable and content assets. This gives AOL the chance to deliver broadband services to many more cable homes.

Moreover, there are fierce internal debates at AOL over strategy: how hard should it push broadband? Should it concentrate on software or content? Mr Logan will probably treat Internet access as a consumer product that needs to be tailored more specifically to different customer groups. Even this, however, will involve changing the mindset at AOL, which long thrived on its one-size-fits-all Internet service.

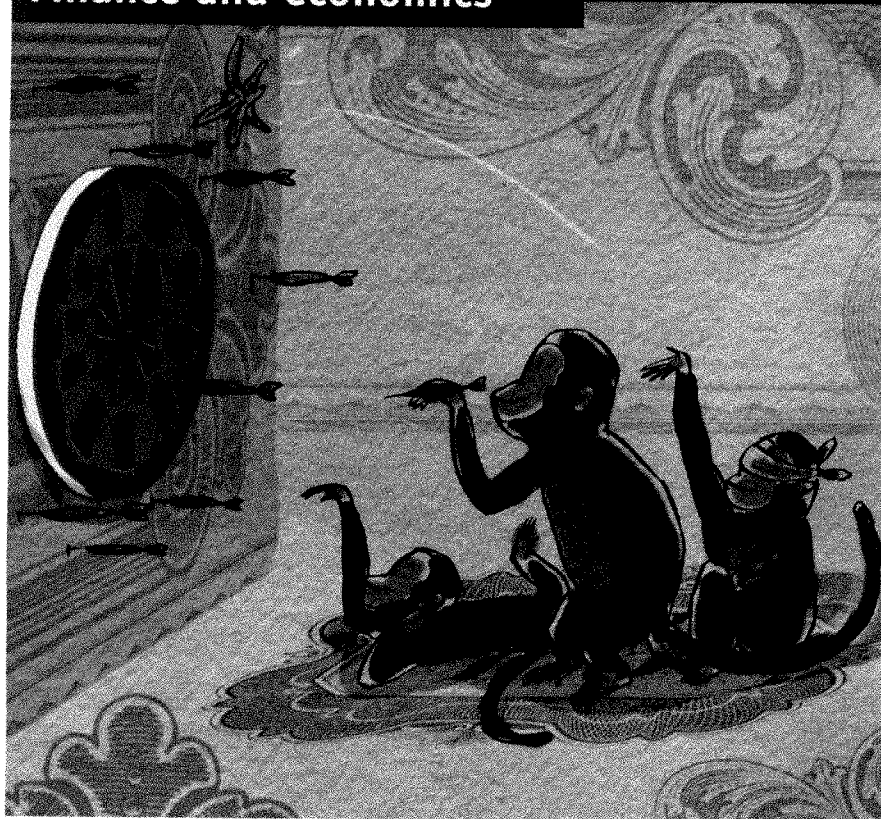
Whether he gets it right or not, Mr Logan's elevation at least satisfies a hunger in the media industry right now for low-key bosses. He can be tough. Yet where Mr Pittman was abrasive and relished the limelight, Mr Logan prefers a good book to a Manhattan cocktail party, and fishing for bass over dining at the Four Seasons. "He'd rather walk than take the company car," says one industry friend. In this, he and Mr Miller are a good match: the antithesis of celebrity executives. As AOL Time Warner battles to restore credibility and turn AOL round, the man who never sought the media limelight will now be squarely in it. ■

Plenty to worry about

AOL Time Warner revenues, by segment, 2001, %



Source: Company reports



Fund management

Mug's game

Does active money-management make any better sense than passive?

EQUITY markets in America and Europe have recently been showing tentative signs of a recovery from their late July lows. Yet investors—in both actively managed funds and in funds that mirror a particular stockmarket index—are smarting still. The average active fund in America has lost over 22% (fund-management fees included) since the end of December 1999, according to Lipper, a company that measures fund performance. In Britain actively managed equity funds have lost 31%. Passive funds, however, have fared even worse, on average. Pure index funds have lost over 27% in America since December 1999, and 32% in Britain.

The choice between active and passive funds is like steering between Scylla and Charybdis, the more so since disillusionment with equities in general set in. Anger is growing—if the newspapers' financial pages are anything to go by—with those who manage mortals' money. Particular scorn has been poured on those poorly performing active managers who claimed that it was precisely during tough times that they would come into their own against indexed funds. In Britain two-

thirds of active fund managers underperformed the index last year, even before the fees that they charged are subtracted. These people are handsomely rewarded for losing money. Each year they pocket 1-2% of the assets they manage, on top of initial charges of as much as 5%. Indexers, by contrast, charge only 0.5% a year, with no upfront fees.

Can't fool all the people all of the time

An average fund manager will beat the market some of the time. Over the long run, though, the great majority of fund managers will do no better than the market average, particularly once their charges are taken into account. The chances are slim of finding one of the blessed few who can show real, sustained skill in stock-picking. Even if you find one, you may discover that what made him good in one economic period will serve him less well in the next.

Believers in the so-called efficient-market hypothesis, developed by American economists in the 1960s, have tried to demonstrate the impossibility of consistent outperformance. They argue that all

useful information that is available to market participants is already factored into a company's share price. Additional analysis of a share by, for instance, taking a closer look at a company's books or talking to its management—as well as all attempts at discovering patterns in price movements—will be futile. Fund management, says the efficient-markets crowd, is a zero-sum lottery in a random world.

This theory opened the door to those offering merely to track the index. The first S&P 500 index fund was started by Wells Fargo in 1973; it held all the stocks in that index. That fund was not open to the general public, but three years later Vanguard, a mutual-fund manager, offered investors an index fund that held all the stocks in the S&P 500 in proportion to their market capitalisation.

Index tracking grew hugely during the bull market of the 1980s and 1990s. In the bear market since early 2000, people have not pulled out much money from index funds—or at least, not yet. In America, the record levels of mutual-fund redemptions in June and July came mainly from actively managed funds. The world's biggest indexer, Barclays Global Investors, with \$400 billion in index funds, claims net inflows (institutional as well as retail money) of \$33 billion in the first six months of this year.

Not everybody buys the efficient-markets hypothesis, however. George Soros, a well-known speculator, thinks he made his money because markets often over- or undervalue things. He also challenges the ►►

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view that share prices are simply a passive reflection of underlying value, or of the expected earnings of a company. A high share price might, for example, trigger certain actions: a public offering of a company's shares, for example, or a merger or an acquisition. A low share price, meanwhile, might stop plans for an initial public offering or a merger. This is what Mr Soros calls the market's "reflexivity".

If knowledge of such a two-way relationship between share prices and assets can be put to good use, a fund manager might consistently do better than the market. Peter Lynch, formerly of Fidelity Investments, showed that a more old-fashioned investment technique—looking for good companies that the market fails for a time to appreciate—can also outperform.

Yet a few examples among a cast of many thousands of fund managers offer only small consolation to the average investor. Unless he wants to punt on fund managers as well as on equities themselves, he will almost always be better off—or, these days, rather less worse off—putting his money into an index fund. ■

Trade

Steel, rolled

A trade war averted, or just a temporary truce?

AS REVERSALS of fortune go, America's steel industry has suffered a big one. Earlier this spring, steel makers got the deal of their dreams when George Bush slapped tariffs of 30% on 12m tonnes of foreign steel. Last month Mr Bush decided to take back some of his earlier gifts. In an attempt to placate Europeans, the administration announced new exemptions for around half the previously affected European steel products.

If betrayal by the White House were not enough, America's International Trade Commission (ITC) has now added insult to injury. In a dispute over imports of cold-rolled steel, a product widely used in the car industry, the ITC ruled that claims of illegal foreign dumping were already being remedied by the Bush tariffs. The commission rejected further attempts to slap on emergency duties. Has America recovered its free-trade credentials?

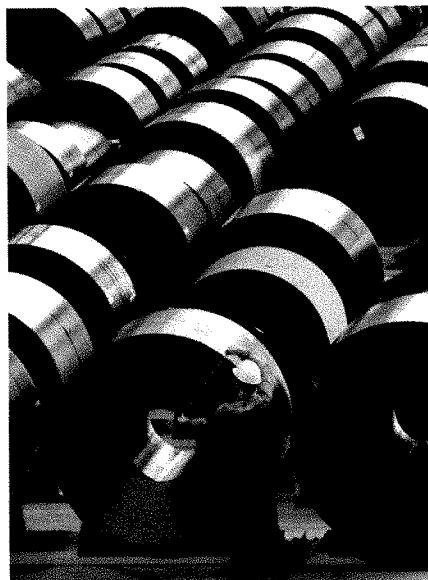
Not quite. The original tariffs are still in place, and still causing pain for some foreign producers. Meanwhile, America's steel makers reap healthy profits these days, as the ITC probably noticed. Even so, the climbdown by the Bush administration, along with the ruling by the trade commission, goes a long way to appease

the European Union, which was on the brink of putting retaliatory tariffs on more than \$2 billion of imports from America.

For now, that threat has receded. The European Union says the latest American moves are welcome. Yet other trade rows rankle. The outrage over America's generous farm bill was not wholly mitigated by its more recent proposal to slash farm subsidies in the Doha round of trade talks. This week's Earth Summit in Johannesburg has put these—as well as Europe's even more generous subsidies—once more under the spotlight. In steel, the cold-rolled case is not yet over. The same charges against 15 other countries are expected to be heard in October, though it would be a surprise if the outcome were different.

Although the steel decisions may mark the end of the worst period in recent EU-American trade relations, nobody is betting on a new golden age of free trade. A new era, however, is about to start at the World Trade Organisation (WTO). This week Supachai Panitchpakdi, a former deputy prime minister of Thailand, succeeds Mike Moore of New Zealand as the WTO's director-general. In 1999, the Americans tried to block Mr Supachai's appointment, but now they insist they are ready to work with him in pushing forward the Doha round. It will, however, take an all-out commitment from America and Europe to get things moving again before next year's ministerial meeting in Mexico. Mr Supachai, for his part, wants especially to promote poor countries' interests.

Shortly after the anti-dumping ruling, Bethlehem Steel, one of the companies bringing the cold-rolled complaint, expressed disappointment. More tellingly, it decided to close a Pennsylvania steel-pipe mill. More closures across the country would do more for the steel industry than going begging to Washington. ■



Taking the measure of tariffs

Gay networks at investment banks

Out and proud

Banks encourage gays to come out

TO JUDGE from stories of nights at lap-dancing clubs, the sexual-discrimination lawsuits and the general atmosphere on trading floors packed with hormone-driven young men, you might expect the culture of an investment bank to be intolerant of homosexuality. In fact, several banks, including UBS Warburg and HSBC, have recently started social networks that seek to support gays and lesbians. Some that have not, such as Morgan Stanley, are thinking about it.

With one in ten people gay, says Jiten Patel, an equality and diversity manager (yes, they really exist) at HSBC, many gays who have not come out at work may waste time and energy worrying about their colleagues finding out. Banks are treating the act of coming out at the office with sensitivity. The networks at HSBC, J.P. Morgan Chase, UBS Warburg, Merrill Lynch and Goldman Sachs allow gay and lesbian employees, some of whom may not have told their families, to join anonymously if they wish.

J.P. Morgan Chase has the oldest gay and lesbian network, with 400 members worldwide, called Pride. It uses the network for graduate recruitment, as do the other banks. Taking the business purpose one step further, however, J.P. Morgan Chase also uses the network to prospect for rich new clients. After Pride sponsored the most recent Stonewall dinner in London, a gay and lesbian event, one founding member, Robert Ioannou, a private banker, says he made several new business leads.

For some banks, starting a gay and lesbian network simply recognises reality. At Goldman Sachs in New York, a group started their own informal network in 1999, before getting official sanction. At Morgan Stanley in the mid-1990s, an unofficial group held cocktail parties in Manhattan and called themselves the BBOMS, or the Beautiful Boys of Morgan Stanley.

What do heterosexuals think? They want to know if the network is really a dating service and who is a member, says the founder of a gay group in London. So far, it is mostly gay men and women in banks' back offices—information-technology and trade-settlement staff—who are joining the networks. However sincere the support from your senior managers, it takes more guts to come out on the trading floor.



Enron and the economics of greed

Prosecutor's dilemma

Enron's prosecutors wonder whether greed is worse than lying

NOW that federal prosecutors have persuaded Michael Kopper (above, left), a former Enron executive, to plead guilty, eyes have turned to his superiors: Kenneth Lay, the bust energy-trading giant's former chairman, Jeffrey Skilling, its former chief executive, and Andrew Fastow (above, right), its former chief financial officer. Mr Fastow seems in particular jeopardy, having made \$30m-odd from running off-balance-sheet partnerships, called special-purpose entities (SPEs), used to keep debt conveniently off Enron's balance sheet. He may be the first of the three to face criminal charges, but for what?

The complaint by the Securities and Exchange Commission (SEC) against Mr Kopper points the way to the arguments that Mr Fastow might face. It makes much of the personal "enrichment" of Mr Kopper and Mr Fastow, and tells a sordid tale of lies used to defraud Enron of millions of dollars racked up by company insiders. Strangely, however, the complaint dwells more on the financial economics than on the specific laws broken to reap the gains.

The SEC's strategy pays unwitting homage to economists' notions of risk and return. This is the idea that big pay-offs come only from taking big risks: the higher the risk, the higher the pay-off. The SPEs in which the two men invested and from which they profited, says the SEC, were not genuine investments at all. Instead, any capital invested was guaranteed by Enron, so Mr Kopper and Mr Fastow were shielded from loss. Thus, the money they got was not a return on their investments,

but merely old-fashioned theft.

To be sure, the sums were generous. Mr Kopper put \$25,000 into one partnership and received \$4.5m. The same gain was reaped by a family trust of Mr Fastow's. To the problems of accounting, disclosure, and conflicts of interest at Enron, the SEC now appears to be adding a fresh charge: getting rich by flouting the laws of risk and return.

Why the new focus? One reason may be that Enron's board authorised Mr Fastow's conflict of interest; its auditors, Andersen, signed off on the accounting of the SPEs. Following ill-gotten money might be the best strategy left to hold Enron's executives responsible. There is some risk to this strategy. If Mr Fastow's winnings are cited in court, he needs only to compare his fees with those of investment bankers arranging mergers and acquisitions, underwriting shares, and putting together fancy financial deals.

Compared with other rainmakers of the late 1990s, Mr Fastow might not look so greedy. Investment banks earned up to 7% in fees for money they helped to raise in initial public offerings. Frank Walsh, a former director of Tyco, took home a \$20m fee for brokering the purchase of CIT, showing how eager other executives were to play at investment banking. This summer, when investment banks carved CIT out of Tyco, they netted \$184m in fees. These returns were all legal, even if you think they were excessive. Prosecutors may have a hard time showing that Mr Fastow's returns were much different. ■

Predatory lending in America

Hunting the loan sharks

Lawmakers, state and federal, are mounting an attack

THE stories of victims of predatory lenders—typically low-income minority families, single mothers and the old—are awful to hear. People are persuaded to take loans priced way beyond their means, usually secured on their homes; eviction is often the price of default. The experience of one woman, a 90-year-old widow from the Bronx who was almost thrown out of her home, inspired Aurelia Greene, a New York state lawmaker, to sponsor a bill to tackle predatory lending. Ms Greene's bill is just one of many. In the past few years tough laws have been passed in North Carolina, Georgia, California and Ohio, and more are on the way elsewhere. Bills loom in both houses of Congress.

As with pornography, consumer activists and legislators say they know predatory lending when they see it. In fact it is tricky, some say impossible, to define particular types of lending as predatory. Most of it is sub-prime, meaning to people with bad or non-existent credit records. The loans carry a higher rate of interest than do prime loans, to compensate for the higher credit risk. What calls itself the sub-prime industry argues that a practice that seems damaging can actually help some borrowers: you have to look at each case, they say, not apply blanket bans. Some people, indeed, argue that except for fraud—false information or faked signatures—there is no such thing as predatory lending, since borrowers are not forced to take the loans.

For years, these arguments kept tough legislation at bay, and the sub-prime market grew from \$20 billion in 1993 to \$150 billion in 1998. In recent years, however, regulators and politicians have been hearing ever more stories of people trapped in debt because of crippling rates and fees. In 1990-98, despite a strong economy and falling rates, the rate of home foreclosures rose fourfold.

Sub-prime lenders are particularly strong in black and other minority areas. According to a study by the Department of Housing and Urban Development, sub-prime loans are five times as common in black neighbourhoods as in white ones. Despite considering anti-predatory lending legislation, Congress is likely soon to pass a new bankruptcy law that would sharply limit consumers' ability to discharge their debts and start with a clean slate. Predatory lending would then become even more of a burden on its victims.

The new laws emerging in states and

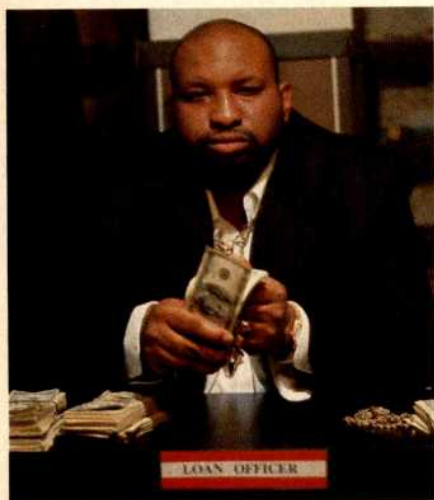
► cities across America try to label certain loan characteristics as predatory, so as to ban them. Most also reduce the thresholds at which a loan is considered high-cost and subject to additional rules. In Congress, a predatory-lending bill sponsored by Senator Paul Sarbanes would prohibit balloon payments, among other things, in which the bulk of a loan is left unpaid at maturity, often without the full understanding of the borrower who then cannot repay.

Mr Sarbanes's law and the others may stop some of the most egregious practices of rogue sub-prime lenders. They will not solve the real problem, which is lack of competition. Despite the sub-prime market's attractive returns, prices have not fallen as others come in. Sub-prime lenders have grown in number, and though they compete with each other for new customers, they do so by spending money on marketing and door-to-door salespeople, not by offering lower prices.

Why is this? According to Fannie Mae, the government-sponsored mortgage-lending agency, up to half the people who take out sub-prime loans could qualify for a prime loan, which charges as much as four percentage points less interest, a huge saving over the 30-year life of a mortgage. The reason that many sub-prime borrowers do not demand prime loans or shop around for the best sub-prime price is a lack of basic financial knowledge.

If sub-prime borrowers could be helped to make better decisions, says James Carr, head of research at the Fannie Mae Foundation, sub-prime lenders would have to bring rates down, and many would get prime loans. Mr Carr wants third-party assistance for borrowers: people who can review loan agreements, advise on how to build a credit record and warn against particular lenders. Such a programme would be cheap, he says, because sub-prime lending is so concentrated in certain neighbourhoods.

Another source of hope for victims of



His payments balloon

Bank accounts in Japan

Open to offers

TOKYO

Why the Japanese have so many accounts

PEOPLE in Japan have eight bank accounts each. According to the Bank of Japan, there were more than a billion individual bank accounts at the end of March, for a population of 127m. These numbers include neither Japan's mammoth postal savings, run by the government, nor the millions of deposits at agricultural co-operatives. With them, the average goes up to at least 13.

That ordinary and savings accounts held at the same bank are counted separately partly explains the phenomenon. But people would still need to bank at several institutions for the number to be so high. Anecdote suggests that worried depositors have recently been splitting accounts among banks, wary of reforms that might cap government protection of bank deposits at ¥10m (\$85,000) per account next April. On the other hand, the average number of bank accounts has barely changed for years.

In fact the high number of accounts per person has more to do with how banks market their services. Perks are often used to attract fresh customers. Jo-

nan Shinkin Bank, a credit union, once offered sacks of rice to new depositors; it now offers ¥100,000-worth of travel coupons in a draw as an enticement. Most of Japan's 700-odd regional banks and credit unions have hordes of salesmen who canvass neighbourhoods persuading locals to open accounts, even small ones.

Although all this creates lots of dormant accounts that cost money to run, banks hope that some, at least, might spawn fresh business. With one popular type of account, called instalment savings, customers promise to put aside a fixed sum that is collected by their banker on monthly visits. The scheme helps customers to save, say, for their dream house, while securing, for the banks, a future piece of mortgage business.

With money spread so widely, it is no surprise that 99% of all deposits, and 70% by value, should be smaller than ¥10m. Delaying deposit-insurance reform, as many politicians in the ruling Liberal Democratic Party hope to do, would benefit few individual depositors, helping corporate, public or rich ones instead.

BRE Bank

Risky rainmaker

WARSAW

Poland's self-styled investment bank gets in over its head

POLAND'S banks are battenning down the hatches. A stumbling economy has hit profits and increased non-performing loans, prompting a more stringent credit policy. The mere thought of providing finance to troubled companies, let alone taking large stakes in them, puts the wind up most Polish bankers. But BRE Bank, a listed corporate bank that is half-owned by Germany's Commerzbank, and that has a much-trumpeted investment-banking business, is a daring lender.

While most analysts scoff at the notion of an investment bank in Central Europe, given the scarcity of capital and big deals, BRE Bank has found a niche in corporate restructuring. A string of transactions, involving the sale of coveted stakes in Polish companies to long-term investors, has turned the bank into the region's best-known dealmaker. As its peers shunned equities, BRE invested with relish.

Much of the excitement has been pro- ►►

vided by Wojciech Kostrzewa, BRE's boss. A veteran Polish banker at 42, Mr Kostrzewa has enjoyed rare freedom for a banker answerable to a foreign owner. Although Commerzbank has a firm grip on the bank's board, BRE has retained its Polish identity—and Mr Kostrzewa has kept his overpowering management style.

After six years heading PBR, a local development bank set up to help restructure state-owned firms, Mr Kostrzewa joined BRE, merged it with PBR and threw it into investment banking and asset management just as the technology boom got under way. In 1999 the sale of a packet of shares in Poland's leading mobile-phone operator, PTC, to Elektrim, a once high-flying conglomerate, was the first of a series of deals that earned BRE spectacular returns that year of 665m zlotys (\$168m).

Since then the flow of deals has been stymied by weak equity markets and economic uncertainty. Investors have balked at BRE's high exposure to technology, media and telecoms firms, and at its heavy losses on investments. That included the cancellation in July of a share offering by ITI, Poland's biggest media company, in which BRE has a 15% stake.

Indeed, many question Mr Kostrzewa's deal-making skills. BRE's stock has sunk to a three-year low, largely because of concern about its own investments, according to Mark MacRae of ABN Amro. August's announcement of a worse-than-expected net loss of 93m zlotys in the first half of this year forced the bank to scrap its end-year profit forecast, one-third of which was to have come from asset disposals. The bank has axed one-sixth of its workforce. A push into up-market Internet banking has won plaudits, but it is still early days.

A retreat from investment banking would please investors, but Mr Kostrzewa was counting on another big deal to save the day. Earlier this year, BRE teamed up with local investors to take control of Elektrim just after the company defaulted on its convertible bonds. In a bid to help the conglomerate stave off bankruptcy (a life-saving deal with its creditors may now have bought it time), the bank agreed to purchase €100m (\$98m) of its short-term debt and was in exclusive talks to buy its telecoms assets, which it later planned to sell to a foreign investor at a hefty premium. Now legal snags at Elektrim appear to have scuppered the deal.

A strong believer in "convergence"—the notion that Polish asset prices will rise as Poland's entry to the European Union gets closer—Mr Kostrzewa is eyeing the power sector. BRE recently joined a local consortium in the running for a cluster of electricity distributors in northern Poland. With Elektrim holding a stake in the second-largest power generator in Poland, BRE's next gamble might just pay off. Provided his customers keep the faith. ■

Global house prices

As safe as what?

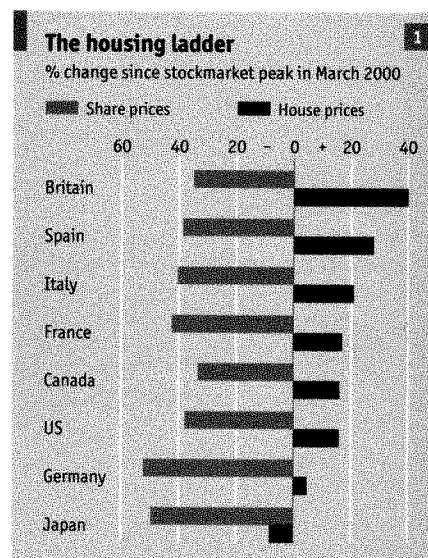
Disillusioned investors have turned from shares to housing. A bubble, anybody?

FOR all the newspaper space devoted to stockmarkets, households around the world have far more of their wealth tied up in property than in shares. American households' shareholdings briefly surpassed the value of their houses in the late 1990s. Now they have about \$11 trillion-worth of shares (held directly or in mutual funds), compared with almost \$14 trillion in housing. In other countries, housing is even more important. In rich countries as a whole, individuals own \$23 trillion in equities, but perhaps \$40 trillion in property.

Property is thus the world's biggest asset class, yet timely data on house prices in different countries is hard to find. That is why, earlier this year, *The Economist* launched its global house-price indicator: a set of house-price indices for 13 countries, going back to 1980, both on an average nationwide basis and for big cities. It is time for a mid-year update.

Almost everywhere, house prices continue to outpace inflation. The exceptions are Japan, where house prices are now in their 11th year of decline, and Germany, where prices have been more or less flat since 1992. Britain has risen to the top of the house-price inflation league, with prices up by over 20% in the year to July, double the pace of a year ago. Australia, Canada and Spain have also seen price gains of at least 10% (see table).

Average house-price inflation in America has slowed to around 7%, from 9% in mid-2001—a rise, still, of more than 5% in real terms. American house prices have risen by more in real terms since 1997 than



in any previous five-year period since 1945. The National Association of Realtors says that house-price inflation has accelerated strongly in many cities in the second quarter. New York, Washington DC and Los Angeles all saw rises in median house prices of 18-22% over a year earlier.

At the other extreme, house-price inflation has slowed sharply in Ireland, Sweden and the Netherlands. These three countries had among the fastest price increases in real terms over the previous five years, and were starting to look distinctly frothy. Irish house prices rose by an annual average of 20% between 1996 and 2001; in the year to June prices rose by just 5%.

Chart 1 compares the change in house prices with the fall in share prices since March 2000, when the stockmarket bubble burst. The canny British investor who sold all his shares in early 2000 and bought a house would have enjoyed a 40% gain in his wealth, compared with a loss of 35% had he stayed in shares.

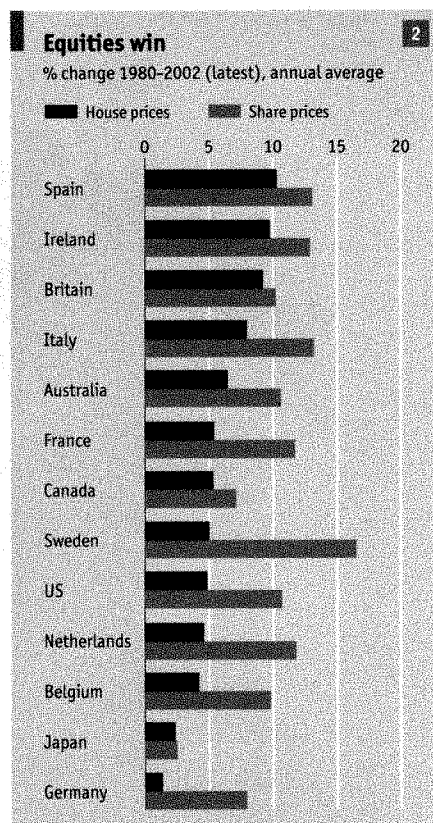
Housing snakes and ladders

If 1980 is taken as a starting-point, however, equities have risen by more than house prices everywhere, despite the bear market (see chart 2 on next page). Martin Barnes at the Bank Credit Analyst, a Canadian research firm, has tracked total returns from housing and shares in America over a longer period, including rental yield and dividends. The total return from investing in property consists not only of a capital gain, but also a rental income or ►►

The Economist's house-price indices

House prices, % change on year ago

	2002, latest	mid-2001
Britain	20.9	9.4
Australia	17.3	8.2
Spain	15.7	15.5
Canada	9.9	4.9
Italy	9.5	8.9
France	8.0	8.1
United States	7.0	9.0
Netherlands	6.4	10.0
Belgium	5.9	5.7
Ireland	5.2	15.1
Sweden	3.6	8.4
Germany	1.6	1.6
Japan	-4.4	-4.1



► benefit from living there (you would otherwise have to rent somewhere else). Mr Barnes finds that investment in American homes massively outperformed shares between 1960 and 1980, but then did badly from 1982 to 2000 (see chart 3). Now housing is outperforming once again.

Unlike most equity investment, most homes are paid for by borrowing; interest payments may offset the rent. But the use of leverage can also greatly boost the return on your initial stake. Suppose you invest \$20,000 in shares, which after five years are worth \$40,000, including reinvested dividends. That implies an average annual return of 15%. Alternatively, you could use the \$20,000 as a deposit on a \$100,000 house, which then rises by an average of 7% a year over five years, to \$140,000. Assume for simplicity that mortgage-interest payments and maintenance costs exactly offset the rental income (or the benefit of living in the house). Then comparing the total capital gain of \$40,000 with the initial stake of \$20,000 gives an annual return of almost 25%.

The more favourable tax treatment of housing adds to its attractions. In many countries, home owners get tax relief on

mortgage-interest payments; more important, owner-occupiers are exempt from capital-gains tax. Against this, the costs of buying and selling a house are far bigger than the cost of trading shares. Taking all this into account, the net return from property, over long periods of time, has in many countries exceeded that from shares.

Traditionally, shares and houses have risen and fallen together. Yet house prices have risen as equities tumbled over the past two years. There are two explanations. With interest rates at 40-year lows, mortgages are unusually cheap. And people increasingly see property not just as a roof over their head, but as the only way left to earn a decent return on investment.

With the value of mutual funds (unit trusts) shrinking, and future pensions looking less secure, many Americans and Britons now see their homes as, in effect, a part of their future pension. They are borrowing more either to buy a bigger house or to buy a second property to let. When they retire they can unlock their wealth in several ways: by selling and moving into a more modest house, by taking out an annuity against the value of the property, or by selling an investment property.

A recent study by the Milken Institute in Los Angeles suggests that, in America, housing has replaced gold as a safe haven in times of uncertainty. This, they say, is why investors have poured money into property as the stockmarket has slumped. The authors find that, from 1945 to 1980, the share of property in households' total assets was positively correlated with GDP growth. Since 1980 they find a negative correlation: housing becomes more attractive at times of slower growth. Until the 1980s, households invested more in housing as equities rose; as shares fell, they put less into housing. By contrast, the recent fall in share prices has seen more money move into housing.

One reason for the change since 1980 is financial deregulation, which has allowed mortgage rates to vary more over an economic cycle, making housing more affordable in downturns. Another is that financial innovation has made property an asset that is easier to tap. A home owner may now convert capital gains into cash by borrowing against the rising value of his house. Home-equity withdrawal (the increase in borrowing in excess of new investment in housing) is running at record levels in both America and Britain.

There are reasons to think that the increased interest in property as an investment is here to stay. Yet there is also a big risk that investors, burnt by the stockmarket, are now overinvesting in housing. The market for housing is almost as prone to irrational exuberance as the stockmarket. And a housing bubble is more dangerous than a stockmarket bubble, because it is associated with more debt. A steep fall in

house prices would harm the global economy far more than a slump in share prices.

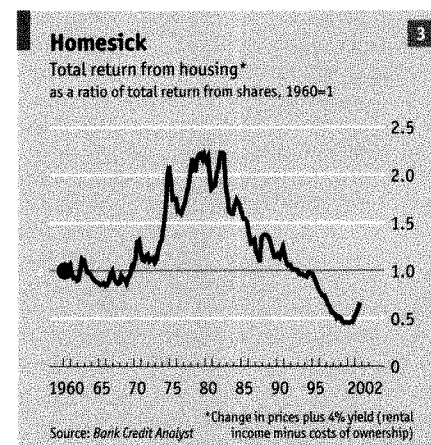
The best gauge of whether house prices are overvalued is the ratio of house prices to average disposable income—the equivalent, as it were, of the price/earnings (p/e) ratio for shares. In America and Britain, this ratio is now close to its peak of the late 1980s, and the ratio is flashing red in some cities, such as London and Washington, D.C. In Ireland and the Netherlands, the ratio is at a record high.

House prices cannot continue rising at today's pace. Yet unless interest rates rise sharply, which seems improbable in the near future, most economists reckon that prices are more likely to flatten off than collapse. Prices appear to be levelling off in London as well as in parts of America.

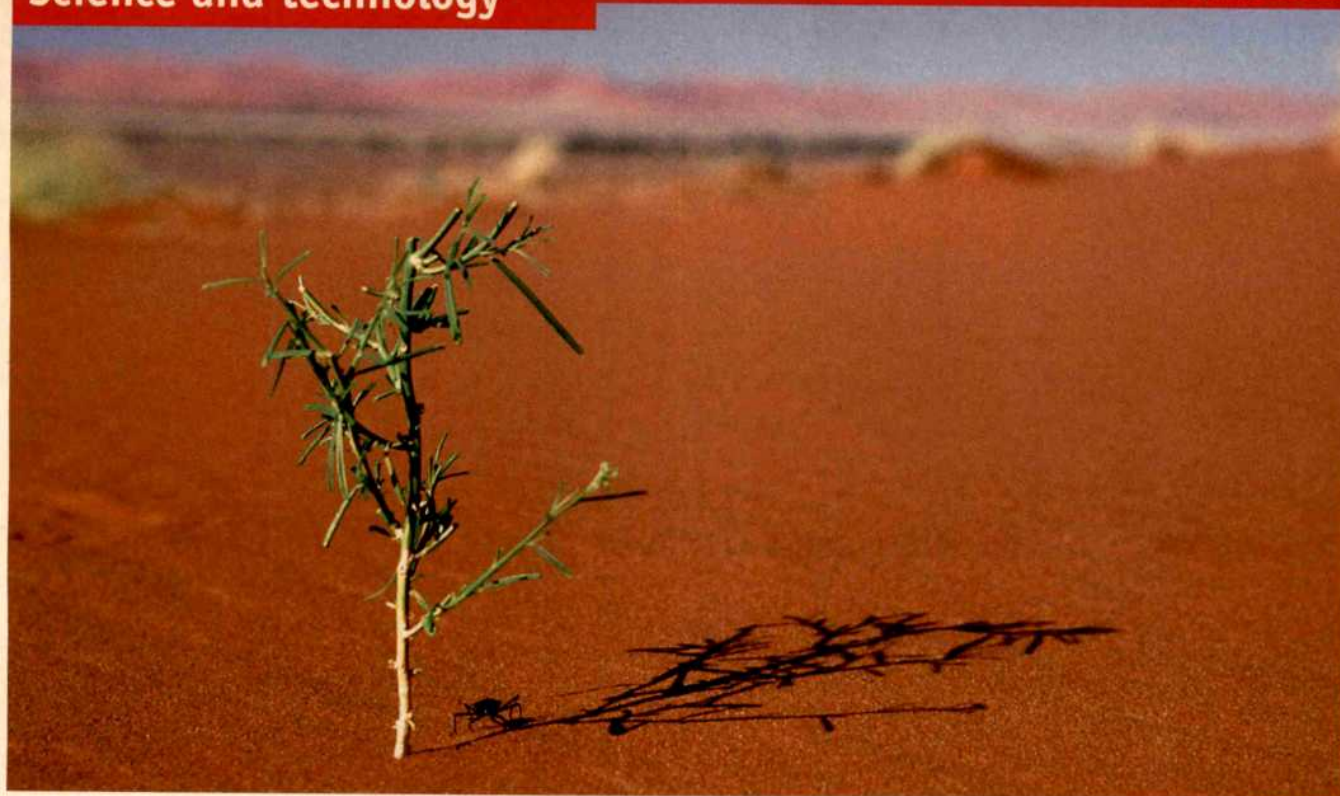
American house-price inflation is likely to slow, yet Mr Barnes expects that housing will continue to outperform shares. The previous two peaks in the ratio of house prices to income happened, he says, when the p/e ratio for shares was low, making shares cheap relative to housing. Today, shares look overvalued, which boosts the relative attraction of housing.

All this means that house prices might continue to rise for a while yet. But the higher they climb, the more households' debt will swell. The real housing bubble in America and Britain is not the rise in house prices, but the growth in mortgage debt, which is at record levels in relation to incomes. The optimistic view is that, with interest rates at 40-year lows, households can afford to borrow more. Still, home buyers may be underestimating the true cost. Interest rates are low because inflation is low. But that means that borrowers can no longer rely on inflation to erode their debts, as it did in the past.

At the very least, households hoping that ever-rising house prices will provide generous nest eggs are likely to be disappointed. At worst, the risk is that prices in many countries may take a tumble. Falling house prices, massive debts and low inflation: now that really would be an unpleasant cocktail to contemplate. ■



We are grateful to the Bank for International Settlements for contributing a large part of the data in this article. Updated statistics were also provided by OFHEO, National Association of Realtors, Japan Real Estate Institute, Nationwide Building Society, Bulwien, Nomisma, INSEE, ESRI, Statistics Netherlands, Statistics Sweden, Westpac, Stadim, Tinsa and Thomson Datastream.



Sustainable development

A few green shoots

JOHANNESBURG

The United Nations' World Summit in Johannesburg is an easy target for cynicism, and rightly so. But it could yet do some good

"THIS is not a sprint, it's a marathon." So said Colin Powell, America's secretary of state, when describing sustainable development. That neatly sums up the opportunities and frustrations presented by the World Summit on Sustainable Development, the successor to the much-vaunted Earth Summit held in Rio de Janeiro a decade ago.

The gathering, organised by the United Nations, got under way this week as thousands of diplomats, activists, businessmen and journalists descended upon the hapless city of Johannesburg. The summit will culminate on September 4th, when over 100 heads of government (not including Mr Powell's boss, George Bush) are expected in town to bless the proceedings.

Because negotiators are busy haggling over everything from trade to aid to technology transfer, it is anybody's guess what the bigwigs will agree to in the end. Even so, one thing is already clear: this is not Rio. For a start, while the elder George Bush attended the Rio conference, his son is happy to give its successor a miss. Also, this summit lacks any of Rio's set-piece treaties, such as the Framework Convention on Climate Change, or the agreements

to stop species loss and desertification, that added sparkle to the earlier summit. That has led some to conclude that the Johannesburg meeting will prove a waste of time. They are not necessarily right. But if governments get it wrong, it will certainly be a wasted opportunity.

The ghost at the feast

"The American way of life is not up for negotiation!" Mr Bush senior was stating the obvious when he uttered these words in Rio a decade ago. However, he set off a furore among greens that was matched only when his son withdrew from the Kyoto treaty on climate change last year. If Mr Bush junior were in Johannesburg next week, as he should have been, he would no doubt say much the same. That may be a reason why the silver-tongued Mr Powell is heading the American delegation.

Scratch the surface, though, and you find reason for optimism: the Bush administration is not, in fact, trying to undermine this summit. It has done things recently that some consider downright supportive. And although Mr Bush is not attending himself, he is sending a well-regarded team of diplomats and experts. Rival nego-

tiators and UN officials say that the American delegates have been, in contrast to their behaviour over Kyoto, "constructively engaged in the process".

What is more, the administration has recently put some surprisingly large sums of money into the pot for international assistance. Mr Bush offered \$5 billion of foreign aid during a recent conference in Monterrey, Mexico, and his officials have since agreed to share in a \$3 billion replenishment of the Global Environment Facility (an agency associated with the World Bank that is a way for rich countries to direct spending towards global environmental problems).

The reason for this softer stance is not that Mr Bush has suddenly turned green. Two other factors explain the volte-face. One is the stinging condemnation heaped upon the president for signing the recent farm bill, which hands out obscene amounts of cash to America's already rich farmers. That backlash overwhelmed the pre-summit negotiations held at Bali earlier this year, and turned them into a fiasco. Since then, the administration has put forward an admirable longer-term strategy for the global reduction of farm subsidies, but many people remain mistrustful of it.

The other motive for America's wish to look a little greener is an indirect consequence of the terrorist attacks on September 11th last year. As Jan Pronk, a former Dutch minister who helped to organise the summit, argues, for America's coalition against terrorism to be successful, "it must have a coalition for something too." Being



Creative destruction

► active on environmental and development issues has a nice, positive ring about it, and this may help to keep a few waverers on side.

Nor need the summit's lack of high rhetoric and grand visions be an obstacle to success. On the contrary: by focusing on the unsexy but essential question of how to implement Rio's grand visions, the people chattering away at Johannesburg may end up achieving rather more. In particular, negotiators seem likely to produce concrete plans for action in three areas where environmental concerns overlap with the concerns of the poor: increasing access to agricultural technology, to clean water and sanitation, and to energy, particularly electricity. The aim is to translate noble aims into plans with targets and timetables attached—and maybe even to provide some money to help things along.

Tool today, till tomorrow

Inside the official hall, questions of land and farming were to the fore. Top of the list was criticism of the sort of subsidies that the American farm bill so generously gives away. As Penny Fowler, an adviser with Oxfam, points out, the markets in sugar, coffee, cotton and other commodities that tropical farmers can grow cheaply are distorted by subsidies of \$300 billion a year to rich-world growers. For sugar alone, the European Union puts 140% tariffs on many imports from Africa, supports its own sugar-beet farmers to the tune of \$1.6 billion a year, and adds insult to injury by dumping surpluses in overseas markets.

There is no realistic belief that the summit will change these policies substantially. Farming interests are too strong for that to happen. (Though a much-trumpeted agreement to "restore the world's depleted fisheries by 2015" might annoy fishermen, another bothersome lobby, if it puts any of them out of business.) Negotiations on phasing out trade-distorting farm

subsidies should take place in the Doha round of trade talks; there are almost no trade ministers at the Johannesburg meeting. But Ms Fowler hopes that the summit will give a "political steer" that guides rich-country policy formation.

Practical suggestions that will not cost votes at home do, however, go down well with rich countries. Several initiatives were unveiled in Johannesburg. For example, a group of researchers led by the Consultative Group on International Agricultural Research and the UN's Food and Agriculture Organisation announced plans for a new Global Conservation Trust. According to Michael Jeger, of Imperial College, London, despite the flurry of recent activity in genetic technology, the genetic diversity of the world's crops is dwindling. The trust will attempt to stop this by bolstering the finances of gene banks around the world. These banks are repositories of seeds, intended to maintain such diversity against an uncertain future.

Separately from this, the World Bank announced a plan to form a panel of experts to tackle the whole thorny question of new agricultural techniques such as genetically modified organisms (GMOs). Robert Watson, the bank's senior scientific adviser on the environment (and, until recently, the head of the UN's Intergovernmental Panel on Climate Change), hopes this panel will re-create the success that the climate-change panel had in arriving at a consensus among scientists on these controversial issues.

One manifestation of this controversy came earlier this month, when Zambia's government banned the import of food aid containing GMOs, even though 2.2m of the country's people are close to starvation in the famine that has much of southern Africa in its grip. The stated reason was worries about the safety of such foodstuffs, despite the fact that they are consumed by millions in North America. In-

deed, the American government is using the conference to try to persuade African governments that GMOs pose no health risks. But Zambia's administration also fears getting caught up in disputes between America and Europe on the GMO question, and would prefer the country to remain GMO-free for the time being, in case its European trading partners should consider its crops "contaminated", and stop importing them.

Nor any drop to drink

If the planting of genetically modified crops is at one end of the controversy scale, the need to help the world's poorest secure safe drinking water and adequate sanitation is at the other. Some 1.1 billion people lack access to safe water, and more than twice as many have no sanitation. The result is that more than 2m die each year from such diseases as diarrhoea. Many more suffer from ailments that sap their health and prevent them working. Even those that do not get sick waste many hours a week fetching dirty water from distant locations. No sane person thinks this is a tolerable state of affairs.

The world's governments have already pledged—in the form of the Millennium Development Goals agreed at yet another summit in 2000—to halve by 2015 the proportion of people in the world who have no access to clean water. The summiteers at Johannesburg are talking of adding sanitation to that target, too. According to WaterAid, a British charity, the returns on investment in water and sanitation together are three times higher than those on the supply of water alone.

Money is inevitably said to be a problem. The UN estimates that, at present rates of investment, universal access to safe drinking water cannot reasonably be expected before 2025 in Asia, 2040 in Latin America and 2050 in Africa. Meeting the Millennium Development Goals would require lifting the present investment rate of about \$16 billion a year in water-related infrastructure to some \$23 billion a year.

According to WaterAid, however, finding money to build infrastructure is not the hardest part. The real difficulty lies in maintaining that infrastructure once it is built. In recent years, a fierce intellectual battle has raged between experts, development banks and activists on the best way to solve this problem. Community-based initiatives, privatisation, cost-recovery pricing and universal subsidies have all been bandied about, with no clear winner. The matter is so sensitive that even Gerard Mestrallet, boss of Suez, a French company with investments in water across the globe, sounds like an anti-market activist. According to him, "water is too essential to life to be a commodity. Public-private partnerships are appropriate, but it is absolutely irresponsible to privatise in develop- ►►

ing countries."

There may be no clear answers at the moment, but South Africa's own experience demonstrates that political will and a willingness to experiment can go a long way. In 1994, the post-apartheid government inherited a system in which 12m out of 38m people did not have access to clean water. Today, that figure is down to 7m out of 42m, and officials hope to have universal access within seven years. The government has achieved this remarkable result with a model that initially met opposition from both development banks and lobby groups. Water is metered and priced, but the small quantity needed for human survival is given away free.

Energy is another area where the Johannesburg summit is likely to produce results—or, at least, aspirations, perhaps in the form of targets for increasing the global share of renewable energy. According to a new report by the International Energy Agency (IEA), some 1.6 billion people have no access to modern energy supplies such as electricity. These people spend a lot of time collecting dirty and unhealthy fuels such as cow dung and wood, and burning them in poorly ventilated houses. As with water, the resultant pollution leads to much suffering. Even more distressing, says Robert Priddle, head of the IEA, is the report's revelation that in 30 years' time existing policies (which involve an investment of \$2.1 trillion in poor-country power supplies) will still leave 1.4 billion people without access to electricity.

Often the quickest way to help such people, most of whom live in remote rural areas, is not to build expensive connections to national electricity grids, but to deploy off-grid "micropower" plants that draw their energy from the environment in the form of wind or sunlight. Wind power is already popular in some rich countries, and is often cost-competitive with electricity from a grid, even if that grid is already installed and is a sunk cost. Solar cells are not yet competitive, although their price is falling. But in many countries the economics of both are stymied, as with agriculture, by subsidies.

Sir Mark Moody-Stuart, former boss of Royal Dutch/Shell, a large Anglo-Dutch oil company, looked into this closely when he served as head of a task-force on renewable energy organised by the G8 group of industrial countries. He stresses the importance of eliminating export subsidies for technologies such as gas turbines and "clean coal" plants.

At first sight that might seem strange. Both of these methods of generating electricity are greener than the traditional ones because their exhausts are not so polluting (in particular they produce less carbon dioxide, and so contribute less to global warming). But they are likely to be used in medium-to-large power stations attached

to grids. They would therefore serve the urban population, which is already "gridded up", and provide little extra incentive to provide power to the countryside. Sir Mark is not necessarily suggesting the total elimination of subsidies, just their redirection. He proposes aiming them at micropower generators that use renewable energy, for example by reducing their price when they are sold to the villagers who need them.

A million points of light

The shift from huge electricity grids to village-owned micropower generators is a reflection of a wider shift that is taking place over how the grand promises of conferences such as the Johannesburg summit are turned into pedestrian reality. If there is one thing that the decade since Rio has made clear, it is that a top-down approach rarely works. Governments cannot deliver on such pledges by themselves. They have to involve their own people, whether as consumers or businessmen—or, frequently, just get out of people's way.

A fashionable, though controversial, move in this direction, which this summit could make less controversial, is so-called "Type 2" partnerships, organised by (or, at least sanctioned by) the UN, and involving governments, businesses, non-governmental organisations (NGOs) and local community groups. ("Type 1" partnerships are government-to-government.)

Such collaborations have happened informally for a long time, of course. But the bureaucrats would like to codify them. That may have advantages. It would, for example, be easier for groups elsewhere in the world to learn from individual successes. But, while business groups such as the World Business Council for Sustainable Development have warmed to them, many NGOs remain sceptical. The most

extreme, such as Christian Aid and Friends of the Earth, scream that business has hijacked the summit. Many anti-capitalist groups are planning to take to the streets of Johannesburg on August 31st.

Not all NGOs are so rabidly anti-business. Dozens have already signed up for Type 2 partnerships with rapacious capitalists to help deliver basic services to the world's poorest people. As Sunita Narain of the Centre for Science and Environment, an Indian NGO, puts it: "I have no problem with the private sector. God, how could anyone from India possibly think that government can solve all our problems?" Her quarrel with the Type 2 deals is more profound. Experience has shown, she argues, that solutions to the environmental problems that plague poor people lie neither with government nor with business, but rather with the poor themselves—if they are given the power to change their circumstances.

It is a nice ideal. But there are limits to what even grass-roots activism can do on its own. If anybody doubts that, they need only visit Soweto. This predominantly poor suburb of Johannesburg sprang into the world's headlines during the protests and bloody repression of the apartheid era. Today, it is fomenting a new protest movement called Operation Khanyisa ("light up", in Zulu).

So which oppressive dictators are the locals fighting these days? Robert Saunders, a local businessman, explains: "We object to these unjust rates and to privatisation. We want no cut-offs for non-payment. We started in Soweto but now have branches all over South Africa!" It turns out their marches and angry slogans are directed at the evil policy of charging users the cost of providing basic services like electricity. The road to sustainability still has a few bumps in it. ■



That looks pretty sustainable



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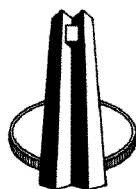
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S O U T H A F R I C A N R E S E R V E B A N K



Mr T T Mboweni, Governor

*The Governor's Address at the
eighty-second ordinary general meeting
of shareholders of the
South African Reserve Bank
on 27 August 2002 can be accessed at*

www.reservebank.co.za



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The history and future of pensions

Matters of life and death

We all want good pensions. But how are we going to pay for them?

LIKE short skirts, fashions in pension reform come and go. In the early 1990s, when the world realised that increasing longevity and low birth rates meant there would be a lot more old folk around in future, the received wisdom was that generous state pensions run on the pay-as-you-go principle—with today's workers shelling out for today's pensioners—would become untenable a few decades hence. By 2050, the forecasters said, the proportion of people over 60 to those aged 15-59 would climb from about 30% now to over 60%. The answer—particularly in the rich countries, but even in the developed world, which was beginning to run up against the same problems—was much greater emphasis on fully funded private provision, which would be fairer to future generations. State provision should be reduced to a bare minimum.

In 1994 the World Bank published a report, "Averting the Old Age Crisis", which for the rest of the decade became the set text for pension reform. It argued that public pay-as-you-go systems were financially unsustainable and should be cranked down. Instead, there should be mandatory, fully funded and privately managed occupational or personal pensions, supplemented by voluntary personal savings. The awful alternative would be hugely increased contributions to state pensions,

Banking on Death or Investing in Life: The History and Future of Pensions. By Robin Blackburn. Verso; 550 pages; \$30 and £20

greatly reduced benefit levels and a higher retirement age.

Alarmed by such a prospect, governments started tinkering with state pension systems to make them less generous. But voters proved curiously resistant to such rational reform. In continental Europe, where state pensions generally made up the great bulk of people's income in retirement, even comparatively minor cutbacks proved highly contentious. And in hard-nosed America, Social Security—the state retirement scheme—once again vindicated its reputation as the "third rail" of American politics: touch it and you're dead.

Meanwhile, though, private provision was making considerable strides. In America, it is estimated that nearly two-thirds of all full-time workers have invested in 401(k) schemes, a way of building up a portable retirement pot that offers considerable tax incentives. Occupational pension funds everywhere were flexing their muscles as big stockmarket investors. That was fine as long as stockmarkets were booming, not so fine when they went into free fall. Many company pension funds

have now discovered that their liabilities exceed their assets. Investing a large part of a corporate pension fund in the company's own shares turned out to be a particularly bad idea: when Enron went bust, many of its employees lost their entire pension entitlement. And because of lower interest rates, the recently retired who are buying an annuity with their accumulated pension money find the income they are getting from it is far lower than they had hoped. Suddenly private pensions look a lot less secure than those much-maligned state pensions.

Robin Blackburn does an excellent job of tracing these recent developments and rehearsing the pros and cons of various systems. Usefully, he includes a short history of pension provision, short because in the bad old days there was not much need for pensions: people generally worked until they dropped dead at an early age. "Banking on Death", a reference to this "mortality bonus" of early pension systems, is actually an odd title to pick for this book because these days most people live long enough to draw their pensions for many years.

The man generally credited with introducing the first universal pension scheme is Otto von Bismarck. Mr Blackburn quotes a fascinating passage from the German chancellor's speech to the Reichstag in 1889 in which he explained the rationale behind it: "I will consider it a great advantage when we have 700,000 small pensioners drawing their annuities from the state, especially if they belong to those classes who otherwise do not have much to lose by an upheaval and erroneously believe they can actually gain much by it."

Nowadays pensions are not explicitly designed to forestall revolution, but demo- ➤

cratic governments risk being punished at the polls if they fail to ensure that their citizens enjoy a comfortable retirement. Given the expense of doing this through a state system, and the recent disappointments in the private sector, how is this to be achieved? The author has a radical solution of his own to put forward, but it is here that he will lose a lot of his readers.

The trouble is that Mr Blackburn, who is a professor of sociology at the University of Essex and the New School University in New York, and for many years edited the *New Left Review*, is not very keen on capitalism. So the pre-funded scheme he wants to set up to provide second pensions for all alongside the state system, while designed to produce the required revenue through normal investment channels, also has some all-singing, all-dancing features meant to turn it into an instrument for improving the world.

Much of the money would come from requiring companies to issue new shares, say up to a value of 10-20% of their annual profits. These would go into pooled funds to which employees would also contribute, according to their means. But the tax concessions to be gained would be confined to those funds that behaved in ethically and socially responsible ways, took account of the wishes of informed citizens and were subject to civic monitoring. So the funds would not always be aiming for the best rate of return, with its attending "free-market mayhem", but for "the progressive socialisation of the accumulation process". More likely, any company faced with the prospect of being stripped of 20% of its profits would go and accumulate elsewhere. Ah well, try again. ■

Britain and India

They wanted their own share

The Indian Mutiny: 1857. By Saul David. Viking Penguin; 528 pages; £20

THE British Raj boasted one tourist site that drew even more visitors than the Taj Mahal. The memorial well at Cawnpore, nine feet wide by 50 deep, greatly appealed to the Victorians' sense of horror and fascination. For down it, on the morning of July 16th 1857, had been thrown the corpses of around 180 British women and children, massacred in cold blood by Indian mutineers the previous night.

It was only the beginning of a brutal spiral of atrocities and reprisals. By the time the mutiny had been crushed, the British had killed many more Indians—though rarely women and children—and in equally degrading circumstances. The



Trust busters in custody

nephew of the Nawab of Farrukhabad, for example, was forced to eat pig meat before being flogged and then hanged; a single tree in the Nawab's province was used to hang no fewer than 130 men from its branches simultaneously.

Historians have long had a problem with the mutiny, over its motives, antecedents and intentions. Was it, as Indian historians tend to aver, the first war of Indian independence in which a people rose simultaneously to throw off the imperialist yoke, or was it—as British historians have argued—merely a limited uprising of misguided sepoys who had been misled into thinking the British were threatening their religions and caste system?

Now Saul David, a fine revisionist historian with a number of thought-provoking books to his name already, argues with conviction that neither explanation is satisfactory and instead presents a fascinating and convincing alternative.

Mr David demonstrates with recourse to an impressive array of evidence amassed in British and Indian archives that the mutiny was led by discontented sepoys who wanted "to replace their British employers with a native government that would, at the very least, provide greater career opportunities and increased pay". Financial considerations, rather than political, racial or religious ones, lay at the heart of the mutiny.

For all that it has a serious academic point to make, and this is undoubtedly an important work of scholarship, this book reads like a novel. Nobody can read the opening chapter, in which the telegraph's warnings are flashed across the Punjab to

save the British in various cantonments from massacre, and then not want to read on. The issue of animal fat being used on cartridges was, it turns out, manipulated by the mutineers to provide a pretext for their uprising, even though it was generally known not to be the truth.

It was the East India Company's monopoly on hiring soldiers, which had forced down wages since the commercial giant had established its dominance on the sub-continent, that the mutineers hated. Their support for various local princes such as the kings of Oudh and Delhi was intended to promote competition in troops' wages. The mutineers were therefore neither early nation-builders nor misguided dupes, but the world's first anti-trust campaigners. Their key demand was for double-pay, which the local rulers soon found they could not satisfy for long.

The stories of heroism and self-sacrifice on both sides of the conflict are thrilling. The siege and relief of Lucknow are rightly part of the Victorian imperial epic, and the author reminds us why. The viciousness with which the mutineers were punished was a stain on the British empire, but it did ensure that the next 90 years saw peace and order.

Mr David believes that the British came much closer to losing India altogether than is usually appreciated. Because they had superior information technology they were able—just in time—to disarm several crucial Indian regiments moments before they mutinied. It is fair to agree with Donald McLeod, the financial commissioner for the Punjab in 1857, who said: "The electric telegraph saved us." But it very nearly did not. ■

Novels of finance

The amorous effects of cash

Extravagance. By Gary Krist. Broadway Books; 288 pages; \$24

Moral Hazard. By Kate Jennings. Fourth Estate; 192 pages; \$21.95 and £10

YOU might think that the boom-bust cycle at the end of the 1990s and its attendant scandals would have thrown up a wealth of novels about innocence, greed and betrayal in the City or Wall Street. In fact, they have been comparatively rare, and these two stories of finance deserve a closer look for that reason alone.

Gary Krist's "Extravagance" straddles parallel worlds: London in the 1690s and New York in the late 1990s. Both are times of speculative boom, each derived from a combustible fusion of new technology ►►

with stockmarket finance. In London's Exchange Alley, "you can purchase shares of a project to make whalebone whips, say or a Sucking-Worm Engine, or special 'or-seshoes made from the finest India rubber, guaranteed to improve any nag's speed". On modern Wall Street, the technology is fancier, but the motives of the financial operators are the same.

William Merrick, the hero of "Extravagance", flits between these 17th and 21st-century scenes. An ingénu in the big city from Devonshire/Indiana, he is driven by a fascination with stock-jobbing and quickly falls in with shifty Exchange Alley/Wall Street types. During the flotation of a new project, greed leads Merrick to betray his uncle and protector. He emerges richer in pocket, poorer in love and somewhat wiser about the world: an ambiguous end to an entertaining work.

Cath, the heroine of Kate Jennings's

"Moral Hazard", also inhabits two mad worlds. Her husband, Bailey, is in a nursing home, stricken with Alzheimer's disease. To pay for his care, Cath, a left-wing freelance writer, takes a job as a speechwriter for Niederdecker, an investment bank. At odds with her new surroundings, she adopts a detached, anthropological approach to the corporate life. She no longer sees skyscrapers as architectural objects, but as "infestations of middle-managers, tortuous chains of command, stupor-inducing meetings, ever-widening gyres of e-mail. I saw people scratching up dust like chickens and calling it work."

When the stability of the bank is threatened by a large hedge-fund failure, the bankers are protected from the consequences of their foolish actions. As Bailey lies dying, the hospital keeps him alive, against Cath's wishes. "Moral Hazard" is a sad, moving and rather bitter novel. In its pages investment bankers are depicted as humourless, amoral bullies and hypocrites, who hide behind slogans boasting of integrity and respect.

As moral satires, neither of these books quite measures up to "Bonfire of the Vanities", Tom Wolfe's 1987 tale of a bond trader's fall, let alone to the 19th and early 20th-century classics about the corrosions of money. But in their different ways each of them captures the exhausted ethos of a late bull market: faced by the reality of the financial world, Mr Krist's youthful hero loses his joyous, speculative verve and Ms Jennings's heroine touches ground in a sort of bleak disillusion. ■

Soccer

Keeping score

World Football Yearbook 2002-3: The Complete Guide to the Game. By David Goldblatt. Dorling Kindersley; 496 pages; £19.99



It's more than laddism

"IS THERE any cultural practice more widespread than football?", asks David Goldblatt, and well he might. Cult or culture, the game is the world's favourite. There are national soccer books galore. Mr Goldblatt's almanac, a mine of football facts and football lore, is truly global.

The book is attractively designed in a break from Dorling-Kindersley's now somewhat dated white background and drop-shadow look. Full colour, cleverly mapped and charted, up-to-date historical data provide a wide survey of world football, classified by country, city and club. Many a pub or office argument can now be settled with ease. No publisher has brought football and its statistics to life in such an imaginative and engaging way.

German fiction

Not a ripping read

Tod eines Kritikers. By Martin Walser. Suhrkamp; 218 pages; €19.90

IT CAN often seem that the only sure way to get a new novel to the attention of the German reading public is a publishing row or literary scandal. This presumably was not what Frank Schirrmacher, the literary editor of *Frankfurter Allgemeine Zeitung*, intended, when in May he explained in his pages—not that anyone had asked—why the paper wouldn't be serialising Martin Walser's latest novel, "Tod eines Kritikers" (Death of a Critic), even though it had regularly so honoured this venerable writer in the past. As the novel's plot involved the apparent murder of a Jewish critic by a German author, it was in Mr Schirrmacher's view, anti-Semitic.

The charge made tidal waves in Germany. *Die Zeit* commissioned five separate reviews; the FAZ gave their man the free-

dom of two broadsheet pages. The consensus seemed to be that while the novel was not guilty of, as it were, classic anti-Semitism—the character of the critic was not attacked because he was a Jew—Mr Walser had exploited his Jewishness as a way to make him unappealing to his readership.

Some persuasive readings—for example Dirk von Petersdorff in *Die Welt*—placed the characterisation firmly in a stereotypical line of "unproductive Jews"; the man has an effigy for a mother, a banker for a father, no known birthplace, he needs to be pointed to something real (German culture) by a veritable German so that he can parasitically and self-aggrandisingly live off it. He cannot even speak German properly, but has an exotic—Yiddish—accent when he says "German" or "writer" or "literature". Some reviewers ironically congratulated Mr Walser on the first anti-Semitic portrayal of a Jew in German literature since 1945.

What pretty much all the reviewers agreed on was that it was a woeful book. Indeed, the farrago about the murder of the critic, who turns out not to have been murdered, followed by some bafflingly dispersive meanderings about the novelist who didn't do the deed, qualify "Death of a Critic" as a work of deep incompetence. The only pages that—unpleasantly—have any life in them are those given over to an attack on the critic, André Ehrh-König, in whom no German reader will have had any trouble in identifying the noted German critic, Marcel Reich-Ranicki.

Mr Reich-Ranicki, whose autobiography was recently translated into English, is a figure of vast power in German letters, and genuinely a household name. After many years on the FAZ—the same FAZ to whom Mr Walser provocatively submitted his book—Mr Reich-Ranicki found his apotheosis on television, where he took his passionate, vehement, rather gladiatorial style to a show called "Das literarische Quartett", which played until recently to large audiences over many years. Posters showed him tearing apart Günter Grass's novel, "Ein weites Feld" ("Too Far Afield") with his bare hands (the German for a bad review is "ein Veriss": a tearing apart or a rip-up). Mr Walser's own large books had suffered many times at his hands.

"Death of a Critic" is an atrocious book, so bad that not even Mr Reich-Ranicki could have wished it worse. It has the predictable effect, moreover, of making you sympathise with the critic. Mr Walser's claims in interviews that he could only write a book "with love" are quite simply nauseating. Meanwhile Mr Reich-Ranicki may even be regretting his frequently-made observation that a writer need not take the trouble to write a good book if his publishers can make so much money with a bad one. Sales of "Tod eines Kritikers" are said to be upwards of 150,000. ■

Edinburgh fringe

Laughing yourself sick

EDINBURGH

Two comedians who are better than their subject matter

WATCHING the customary parade of penis contortionists, lesbian dwarf cabaret singers and one-legged, satirical performance poets at this year's Edinburgh Fringe Festival may leave you feeling that humankind ran out years ago of things to say about human genitals, terminal illness and the Taliban. On this overcrowded terrain, Trevor Stuart and André Vincent are exceptions. One deals in bodily functions (sexual and scatological), the other in misfunctions (cancer). As with all good comedy, it's less what fluids they talk about—or spill—than how they do it.

To start his show "Taboo", Mr Stuart enters conventionally enough, dressed in a straitjacket and dragging a ghetto blaster on a skateboard tied by string to his most vulnerable member. He then assaults the crowd from behind the disguise of a deranged patient posturing as a psychiatrist. This unashamedly cheap theatrical device gives the good doctor a licence to exploit every uncomfortable subject in the most uncompromising, retch-making ways.

Mr Stuart's success as a manipulator of

audience sensibilities owes less to his cesspool of profanity than to his performance skills. His bizarre stunts and phantasmagoric wit, which simultaneously evoke a sideshow at a Victorian fairground and a theatre-of-cruelty happening, are all delivered with the impeccable timing and physical accuracy that come from training at the Etienne Decroux mime school.

Sado-masochistic and illness-based stage comedy has a distinct tradition. There was the late Bob Flanagan, a sufferer from cystic fibrosis who turned self-punishment into a performance art. There is the Jim Rose Circus, a modern-day freak show that shocks and revolts, and has acquired worldwide notoriety. Using words rather than sick bags, Peter Cook and Dudley Moore, two British comedians, created entire routines about cancer. And when Tom Green, a popular MTV comedian, succumbed to testicular cancer in 2000, he joked about it on screen.

Dying unpleasantly is the material of Mr Vincent's autobiographical comedy. In the cancer ward of a grubby North London



Trevor Stuart's gloves-on humour

hospital, he is wondering what will happen to him next. He was diagnosed with diabetes following a 46-hour drinking binge at the 2000 Edinburgh Fringe, and during last year's festival he was rushed into hospital with cancer of the kidney.

In "André Vincent Is Unwell", the recently resurrected comedian cleverly dissects his own experience on the operating table, recalling, with fascinating detail, every aspect of the process of being ill, from his diagnosis to what the comedian would have us believe is the biggest joke in the NHS—aftercare.

Stopping en route to tell us about his South Park-patterned pyjamas, his experiences at a sperm bank and with broccoli—his grandmother's answer for all ailments—Mr Vincent smatters his narrative with statistics that only a career-invalid would know. These range from the chances he has of dying of cancer (0.03%) to the fact that there are more than 350,000 cancer diaries on the Internet.

What separates this stand-up comedian from others who look for humour in a tumour, is an ability to sustain a single narrative for over an hour with malignant wit. Unlike others who meander, Mr Vincent sticks to his difficult story like a growth to the kidneys.

This isn't for everyone. Squeamish playgoers, or those who simply do not want to pay to be disgusted, may long for Messrs Stuart and Vincent to crawl back to the nursery cots or hospital wards whence their comedy came. To judge from the reactions of the audience, though, others hugely enjoy these two gifted comedians, who deftly exploit the mirth and meaning of sick minds and bodies. ■

John Cage

Listen hard

Silence is golden

ALTHOUGH 50 years old, John Cage's piece for silent piano still reverberates. Lasting four minutes and 33 seconds, it called for no intentional sounds. At the 1953 premiere of "4'33'", given by David Tudor in Woodstock, New York, at the Maverick Concert Hall—a rough, wooden structure open at one end to the woods—there were the sounds of a breeze, then the first drops of a light rain on the roof and finally, the composer said many years later, "the voices of disturbed listeners, some of whom may be said to still be walking out".

For a special concert at the Maverick on August 24th (five days before the actual anniversary), Margaret Leng Tan, a remarkable pianist who has just released a CD with little-known early Cage works of startlingly beauty and jazziness, chose a toy piano not to play. She faced it artfully, with eyes closed. It was a cold, damp night but without the swish of breeze or patter of rain. Re-

spectful, memorial silence ended at last when someone accidentally dropped a plastic water bottle and generated a gratifying bit of audience titter.

The point perhaps of "4'33'" is that we can never experience true silence. There is always something to listen to; even in a sound-proof room we hear the activities of our bodies. When "4'33'" isn't, itself, making an audience mad, it offers a way to welcome the ambient sounds that often otherwise hinder the listening to music at a concert.

It is a tribute to Cage, who died ten years ago, that his avant-garde classic remains musically—and commercially—controversial. In June, a British pop music producer and composer, Mike Batt, made news by getting into trouble with Cage's New York publisher, C.F. Peters. He had included a blank, one-minute cut of silence, attributed to Batt-Cage, on the debut record of The Planetas, a cross-over band, without intending to pay royalties.



THE CONRAD N. HILTON FOUNDATION INVITES NOMINATIONS FOR THE 2003 CONRAD N. HILTON HUMANITARIAN PRIZE

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DEADLINE FOR NOMINATIONS IS NOVEMBER 1, 2002.

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Robert Borkenstein

Robert Borkenstein, inventor of the breathalyser, died on August 10th, aged 89

WHEN Robert Borkenstein became a policeman in the 1930s, a motorist would need to have been clearly drunk before being thought a menace. Unless his speech was unmistakably slurred and he was a bit wobbly on his feet he could probably avoid prosecution. Even if he were taken to court, a lawyer might argue successfully that his client was tired through overwork. Worse, many Americans, happy to have got rid of prohibition, saw a drunk as simply a sociable fellow, a bit of a comic, even at the wheel of a car.

This was not the view of Mr Borkenstein. As a photographer for the Indiana police he had recorded a number of fatal accidents involving drivers that he was sure had drunk too much. When he became head of Indiana's police laboratory he puzzled over the problem of how to measure, simply and reliably, how much alcohol a driver had consumed.

A friend of his at Indiana University, Rolla Harger, was studying the effects of alcohol on humans. He worked out that the amount of alcohol in a person's blood could be measured by taking a sample of his breath. One millilitre of alcohol in the blood equalled 2,100 millilitres of breath. Helped by Mr Borkenstein, he devised an instrument they called the drunkometer. This was the forerunner of the breath-

alyser that Mr Borkenstein patented and marketed in 1954 and which for many years has been routinely used by police in the United States and other countries.

There is often an air of suspicion over claims to the authorship of scientific discoveries, especially those that have resulted in fame and fortune. Was Harger the real inventor of the breath test? He was a pioneer in the study of inebriation, and the drunkometer was an attempt to put his work to practical use. But it involved blowing into a balloon, which was then sent to a laboratory where the air was passed through a solution that changed colour if alcohol was present. The amount of alcohol could then be calculated. The breathalyser was fairly easy to use and could give a quick reading. Our picture shows Mr Borkenstein demonstrating it in the 1970s. Rolla Harger (who died in 1983, aged 93) admired the breathalyser and was happy to credit Mr Borkenstein with its invention. They remained good friends with the common aim of stopping drunken driving.

No lies

Robert Borkenstein was largely self-taught. As a youngster he dabbled in science and devised a system of colour photography. Science, he believed, could defeat the law-breaker. Not only would

science deter drivers from drinking, it would make evidence presented to the courts more reliable. He worked on improving the efficiency of the polygraph—the lie detector—and conducted some 15,000 tests with the instrument. But despite a successful career in the police, Mr Borkenstein felt he had missed out by not having had a university education. He gained the comfort of a degree in his late 30s, in subjects that came easy to him, police administration and French: his wife was French, and the couple often took their holidays in France. Eventually, he said goodbye to the police and took his experience to Indiana University where he became head of its department of forensic studies for 30 years.

As the inventor of the breathalyser, a name that went into the dictionary, Mr Borkenstein was in much demand as a speaker in a country in love with the car but appalled by the carnage on the road. Thousands of breathalysers were made by various manufacturers under licence, increasingly compact and increasingly efficient. One, a coin-machine designed by Mr Borkenstein for use in bars, would speak a variety of messages depending on the state of the user: "Be a safe driver", "Be a good walker", or "You're a passenger".

Competitors to the breathalyser, and claimed to be more efficient at measuring alcohol, are now on the market. Still, the effect of alcohol on the body remains not wholly understood. A study carried out by Mr Borkenstein in 1981 suggested that in certain cases a driver who had drunk less than two ounces of alcohol might be safer than a driver who was an abstainer, because he was more relaxed. The study was paid for by a liquor company and treated with suspicion. Mr Borkenstein was upset that his honest finding was applauded by motorists who said they drove better after a few drinks. He liked a drink, wine especially, but whatever might be its relaxing qualities in some situations, he advocated abstinence at the wheel.

It was a disappointment to him that although the threat of being breathalysed must have deterred many drivers from drinking, the number of road deaths attributed to alcohol remains high: 15,700 in the United States in 1999, more than a third of all road deaths. In Europe the fatalities are proportionately lower. Even so, about 5,000 people die on the roads in Spain each year as a result of drink. Even Sweden, where the legal limit is tiny and drunken drivers routinely go to jail, there are 500 road deaths a year attributed to drink. The Swedes are experimenting with a device fitted to a car dashboard that monitors the driver's breath. If he has been drinking, the car won't start. It may be the next step forward from Mr Borkenstein's breathalyser of 50 years ago. ■



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art, science & business

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That could be you. For more information and an application form, please write to Capita RAS, Innovation Court, New Street, Basingstoke, Hampshire RG21 7JB or telephone the NHS recruitment hotline on 01325 745839 (24 hours). Please quote reference B6723. Closing date: 20th September 2002. You can also apply via www.capitaras.co.uk/nhs

We welcome applications from a wide range of people - men and women, people from different ethnic backgrounds, mature candidates, people with a disability and others.

Call for International Competitive Bidding**Improving Product Quality
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The Common Fund for Commodities (CFC) invites bids from consultants or consulting companies to reformulate and design a project on shea butter in Sub-Saharan Africa (Burkina Faso, Central Africa Republic, Mali and Senegal). The detailed Terms of Reference can be accessed on the website www.common-fund.org under "consultancies".

The consultant is expected to submit a draft in English by 10 November 2002 and the finalised report not later than 25 November 2002. Offers should be sent in writing, to be received by 13 September 2002, to the following address:

The Managing Director
Common Fund for Commodities
P O Box 74656
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The Enterprise Development Department is focused on the promotion of pro-poor economic growth through increasing income opportunities – and our advisers generally work in wider teams tackling private sector development issues, including finance, business development, and enabling constraints. This will be the environment you will join – working primarily on SME finance and microfinance issues, but also playing an important role in pro-poor economic development issues.

In a broad sense, financial development will obviously be a key area for you – and within that micro, small and medium enterprises will take priority. On microfinance, we will look to you for a lead on savings and credit at the household and enterprise levels – and you will work with a number of world agencies on this issue. On SME finance, international policy and best practice work will occupy you, and you will become a focal point on financial sector issues for the DFID network and advisers covering country programmes.

With strengths in communicating, liaising with other bodies and colleagues, analytical thinking and managing people, you will have spent at least ten years working in international development – gathering a significant amount of experience of financial services issues and possibly development agency knowledge. A good first degree and a masters degree or professional qualifications will be important – probably in business

management, economics, finance or banking. And you will be well-versed in financial services, business enabling environments, trade and investment, and business development services. The postholder will be expected to travel for up to 75 days each year.

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For more information on this vacancy, DFID in general, and an electronic application form, visit our website. Alternatively, call 01355 843842 or email hrod3c1@dfid.gov.uk to request an application pack – quoting reference AH 375/3/AF.

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For further details and application procedure please visit the Centre's web site at: <http://www.itcilo.it/english/bureau/turin/jobs/index.htm>. Applications by e-mail are encouraged and the deadline for receipt is 25 September 2002.

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Please send your application, including cv, list of publications, research agenda and proposed period of stay, to The President, Hamburg Institute of International Economics (HWWA), Neuer Jungfernstieg 21, 20347 Hamburg, Germany. Applications are accepted at any time. For further information please contact hwwa@hwwa.de, subject: visiting fellows.

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Danish Ministry of Foreign Affairs Danida

Invitation to pre-qualification Procurement Agents

As part of its efforts to reducing poverty through the promotion of economic growth with poor population groups as active participants, equal participation of men and women, popular participation in the development process as well as the strengthening of the rule of law and good governance Danida is planning to integrate procurement agents in the procurement of goods under its bilateral grant assistance.

Scope of Work

On behalf of Danida the procurement agent will buy local as well as imported goods required in connection with Danida's bilateral grant assistance to its programme countries being Bangladesh, Benin, Bhutan, Bolivia, Burkina Faso, Egypt, Ghana, Kenya, Mozambique, Nepal, Nicaragua, Tanzania, Uganda, Vietnam and Zambia.

The total annual Danida grant budget for its programme countries is approximately 3.8 billion DKK of which a minor part is used for the procurement of goods.

Danida will tender a Programme Country Enabling Agreement (PCEA) for each programme country. Based upon the PCEA the procurement agent will negotiate procurement agreements with the local Danish Embassy and when feasible also with Danida supported projects and sector programmes.

The remuneration of the procurement agent will partly be a management fee and partly transactional fees. It is envisaged that the PCEA will be for two years commencing late 2002. There will be possibility for a negotiated extension of the PCEA of up to further three years subject to satisfactory performance in the first two years.

Qualifications

The prospective procurement agent should demonstrate the following competences and capacities:

- Recent experience with assignments of similar nature and complexity
- Access to experienced and highly qualified local, expatriate as well as headquarter based procurement staff
- Financial viability
- Reputation for efficient and transparent execution of procurement agreements
- Knowledge of the Danish business sector

Pre-qualification will be limited to qualified firms or joint ventures which are legally incorporated in, and have their principal place of business in one of the member countries of the European Union.

Submission of pre-qualification documents

Further information as well as application forms are available at www.um.dk/danida/erhvervsliv/kontraktsekretariatet/pkval.asp

Applications for pre-qualification should reach the Ministry of Foreign Affairs, Asiatisk Plads 2, DK-1448 Copenhagen K, attn Mogens Strunge Larsen or by e-mail to pq@um.dk no later than 13 September 2002.



STATE OF QATAR

Ministry of Municipal Affairs & Agriculture

QATAR PRIMARY ROUTES – DOHA EXPRESSWAY

NOTIFICATION FOR PRE-QUALIFICATION OF INTERNATIONAL CONTRACTORS
SPECIALIZING IN THE DESIGN & BUILD OF MAJOR HIGHWAYS AND BRIDGES PROJECTS

INVITATION TO PRE-QUALIFY

The Government of the State of Qatar represented by the Roads Department of the Ministry of Municipal Affairs and Agriculture will pre-qualify International Contractors with experience of major highway works for the Doha Expressway contract forming part of the Qatar Primary Routes project. The contract will be a Design and Build contract and the successful tenderer will be responsible for the detailed design and construction of the works.

BRIEF DESCRIPTION OF THE WORKS

The Doha Expressway, approximately 50km in length, is one of the most important and prestigious projects in the development of the Qatar highway network. The scope of work includes the detailed design and construction of a 6-lane urban expressway and an 8-lane rural expressway that will enable smooth traffic movement from Wakra-Mesaieed, in the south, to the northern regions outside the capital. Beginning in Mesaieed, the Doha Expressway will pass through Wakra and then intersect with D-Ring, E-Ring and F-Ring Roads in Doha before linking with the North Road. International standards will be applied for the design of grade-separated interchanges, bridges and underpasses. This will facilitate north-south traffic movement and connect the New Doha International Airport with the Qatar highway network as well as improve traffic flow and cargo transportation between the major roads.

THE PRE-QUALIFICATION DOCUMENTS

Pre-qualification documents will be available for collection from the Roads Department, Main Projects Division, Ministry of Municipal Affairs and Agriculture, at the address noted below between the hours of 08:00 to 12:00 noon, upon payment of a non refundable Fee of Qrs.5,000 payable to the Cashier at the Revenue Section of the Department of Financial Affairs, Ministry of Municipal Affairs and Agriculture.

SUBMISSION OF PRE-QUALIFICATION DOCUMENTS

International Contractors that meet the Pre-qualification requirements are to submit the Pre-qualification documents in duplicate no later than 12 noon on Wednesday 30th October 2002 to the Ministry of Municipal Affairs and Agriculture in sealed waxed envelopes marked "Qatar Primary Routes-Doha Expressway" and addressed to:

The Ministry of Municipal Affairs & Agriculture
Roads Department, Main Projects Division
P.O. Box 22188, Doha, Qatar.

Documents received after the closing date and time will not be considered.

Inquiries: All enquiries are to be directed to Roads Department,
Main Projects Division, Ministry of Municipal Affairs and Agriculture.
Tel: (+974) 435-7896. Fax: (+974) 432-1967. Email: qpr@mmaa.gov.qa

UKRTRANSNAFTA

State Oil Pipeline Company of Ukraine REQUEST FOR PROPOSAL

Title: Odessa-Brody Project – Business Developer

Ukrtransnafta invites experienced international business development groups to submit proposals to commercialize the Odessa-Brody Project with international participation and to implement the suggested commercial plan.

Background

A new pipeline and marine terminal system was completed in Ukraine extending from Yuzhnyi port, 35 km east of Odessa, to Brody, a junction of the Southern Druzhba Pipeline. This system was designed to transport crude oil reaching the Black Sea from Eurasia directly to Central European refining markets and beyond without transiting the Turkish Straits. Immediate commercial opportunities also exist to utilize the marine terminal and associated tank farm for transshipment. Current system capacity is 14.5 mta or 290,000 bpd. Ultimate capacity is 45 mta or 900,000 bpd.

Scope of Work

- a) Plan phased development of the project, including expansions and extensions.
- b) Build business and financial cases.
- c) Attract international shippers, offtakers, investors and lenders.
- d) Design and negotiate business structures and commercial terms.

Qualifications

International petroleum, financial, legal, negotiating and management skills with proven track record for executing major, complex and cross-border projects.

Expressions of Interest

The full RFP document will be available at the Ukrtransnafta website www.ukrtransnafta.com. All inquiries are to be directed to the office of the Chairman of the Board, Ukrtransnafta at Email: office@ukrtransnafta.com or Fax: +38-044-246-8377 with a brief Capability Statement. A formal response to the RFP is expected by September 23.

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Overview

American consumers may be losing heart. The Conference Board's consumer-confidence index fell by more than expected in August to 93.5, its lowest since November 2001. Chain-store sales also fell by 1.6% over the first three weeks of August, compared with the first three weeks of July. But Americans ordered more durable goods last month than expected. Seasonally adjusted, orders rose by 8.7% in July, after falling by 4.5% in June. Orders for capital goods leapt by 10.5%, the largest monthly jump since 1992: a sign that businesses might be starting to invest again, even as consumers flag.

Although Americans have been pulling record amounts of money out of equity mutual funds, they are increasingly enthusiastic home buyers. The Commerce Department reported that new-home sales in July jumped by 6.7%, a record rise. Sales of existing homes rose by 4.5%.

The **euro-area** economy grew for the eighth consecutive month in July, but the pace of growth continues to slacken, according to the Centre for Economic Policy Research. That body's euroCOIN indicator of euro-area business activity fell to 0.504 in July from 0.513 in June. Any reading above zero indicates expansion. The euro area's current account recorded a \$24.8 billion surplus in the year to June; it was in deficit by \$43.3 billion in the same period last year.

Germany's Ifo business-climate index fell for the third month in a row, to 88.8 in August, down from 89.9 in July. **Spain's** GDP grew by 2.0% in the year to the second quarter; although household consumption slowed in the second quarter, fixed investment picked up. **Belgium's** economy grew by 0.3% in the year to the second quarter.

In **Sweden**, industrial production fell by 1.3% in the year to June. Unemployment edged up to 4.3% in July, from 4.0% in June.

America's stockmarkets fell sharply. The Dow Jones Industrial Average was down by 2.9% over the week. The Nasdaq fell by even more. Bourses in Europe followed America's lead. The FTSE 100 fell by 2.1%, after briefly posting a seven-week high.

Britain's GDP grew at an annual rate of 2.4% in the second quarter, slower than previously thought. Disappointing manufacturing-output figures for June were responsible for most of the downward revision.

Data on more countries are available to subscribers on www.economist.com

Output, demand and jobs

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production latest	Retail sales (volume) latest	Unemployment % rate	
	1 qtr*	1 year	2002	2003			latest	year ago
Australia	+ 3.6	+ 4.2 Q1	+ 4.0	+ 3.8	+ 4.3 Q1	+ 6.3 Q2	6.2 Jul	6.9
Austria	+ 0.3	- 0.6 Q1	+ 0.9	+ 2.6	+ 2.5 Jun	- 0.2 May	4.1 Jun	3.5
Belgium	+ 0.8	+ 0.3 Q2	+ 1.3	+ 2.9	- 4.1 Jun	- 3.3 May	11.8 Jul†	11.1
Britain	+ 2.4	+ 1.2 Q2	+ 1.7	+ 2.9	- 6.6 Jun	+ 4.5 Jul	5.1 Jun‡	5.0
Canada	+ 6.0	+ 2.1 Q1	+ 3.3	+ 3.5	+ 0.5 May	+ 4.3 May	7.6 Jul	7.0
Denmark	+ 1.4	+ 1.1 Q1	+ 1.6	+ 2.4	+ 4.2 Jun	+ 4.1 Jun	5.1 Jul	5.1
France	+ 1.8	+ 0.4 Q1	+ 1.4	+ 2.7	nil Jun	- 2.5 Jun	9.0 Jun††	8.6
Germany	+ 1.1	+ 0.1 Q2	+ 0.7	+ 2.3	- 2.3 Jun	- 5.2 Jun	9.9 Jul§	9.3
Italy	+ 0.9	+ 0.2 Q2	+ 1.0	+ 2.5	- 5.4 Jun	- 0.8 Jun	9.0 Apr	9.5
Japan	+ 5.7	- 1.6 Q1	- 0.3	+ 1.1	- 2.9 Jun	- 3.5 Jun	5.4 Jun	4.9
Netherlands	+ 0.5	+ 0.1 Q2	+ 1.0	+ 2.5	- 3.0 Jun	- 2.1 May	2.4 Jul**	2.0
Spain	+ 1.8	+ 2.0 Q2	+ 2.1	+ 3.0	- 4.4 Jun	na	11.5 Jun	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.7	+ 2.9	- 1.3 Jun	+ 4.5 Jun	4.3 Jul†	4.2
Switzerland	+ 0.7	+ 0.2 Q1	+ 1.0	+ 2.3	- 8.8 Q1	- 3.0 Jun	2.6 Jul†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.7	+ 3.4	+ 0.2 Jul	+ 5.4 Jun	5.9 Jul	4.6
Euro area	+ 1.3	+ 0.3 Q1	+ 1.1	+ 2.6	- 1.2 Jun	+ 0.7 May	8.4 Jun	8.0

*% change at an annual rate. †Not seasonally adjusted. ‡April-June; claimant count rate 3.1% in July. §EU harmonised rate 8.3%. **May-Jul. ††Revised series.

Prices and wages

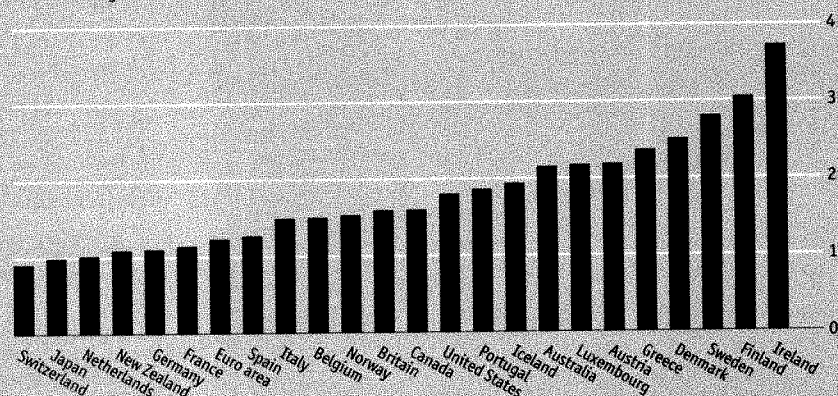
% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2002	2003	latest	year ago	latest	year ago
Australia	+ 2.8 Q2	+ 6.0	+ 2.8	+ 2.6	- 1.1 Q2	+ 5.6	+ 3.7 Q2	+ 4.4
Austria	+ 1.6 Jul	+ 2.8	+ 1.7	+ 1.7	- 1.0 Jul	+ 1.9	+ 2.4 Jul	+ 2.8
Belgium	+ 1.3 Jul	+ 2.7	+ 1.7	+ 1.6	- 0.2 Jul	- 0.4	+ 2.6 Q2	+ 2.6
Britain	+ 1.5 Jul	+ 1.6	+ 1.9	+ 2.4	+ 0.3 Jul	- 0.1	+ 3.9 Jun	+ 4.7
Canada	+ 2.1 Jul	+ 2.6	+ 1.7	+ 2.2	- 1.2 Jun	+ 1.5	+ 2.8 May	+ 0.7
Denmark	+ 2.2 Jul	+ 2.4	+ 2.3	+ 2.0	- 0.9 Jul	+ 2.7	+ 4.0 Q1	+ 3.8
France	+ 1.6 Jul	+ 2.1	+ 1.8	+ 1.4	- 1.5 Jun	+ 2.3	+ 3.9 Q1	+ 4.3
Germany	+ 1.0 Aug	+ 2.6	+ 1.4	+ 1.2	- 0.8 Jul	+ 2.2	+ 2.5 Jun	+ 1.9
Italy	+ 2.3 Aug	+ 2.8	+ 2.3	+ 1.9	- 0.8 Jun	+ 2.4	+ 2.4 Jun	+ 2.7
Japan	- 0.7 Jun	- 0.8	- 1.0	- 0.5	- 2.2 Jul	+ 0.7	- 3.2 Jun	+ 2.1
Netherlands	+ 3.5 Jul	+ 4.6	+ 3.6	+ 2.3	- 2.2 Jun	+ 4.3	+ 3.0 Jun	+ 5.1
Spain	+ 3.4 Jul	+ 3.9	+ 3.3	+ 2.7	+ 0.6 Jul	+ 2.0	+ 4.0 Q1	+ 3.4
Sweden	+ 2.2 Jul	+ 2.9	+ 2.4	+ 2.1	- 0.8 Jul	+ 2.1	+ 4.1 May	+ 3.6
Switzerland	- 0.1 Jul	+ 1.4	+ 1.0	+ 1.2	- 1.6 Jul	+ 0.2	+ 2.5 2001	+ 1.3
United States	+ 1.5 Jul	+ 2.7	+ 1.6	+ 2.2	- 1.1 Jul	+ 1.4	+ 3.2 Jul	+ 4.1
Euro area	+ 1.9 Jul	+ 2.6	+ 2.1	+ 1.6	- 1.1 Jun	+ 3.2	+ 3.3 Q1	+ 2.8

Labour productivity in the private sector

The fastest-growing OECD economy in recent years, Ireland's, has also enjoyed the fastest rate of growth in productivity, defined as output per worker. At a forecast 3.7% a year between 1993 and 2002, Irish productivity growth, driven by strong foreign direct investment, has been twice America's. Nordic countries have been the next best performers, but Switzerland and Japan have seen only weak productivity growth.

Annual average % increase 1993-2002*



Source: OECD

*Forecast

Money and interest rates

	Money supply*		Interest rates % p.a. (Aug 28th 2002)					
	% change on year ago		3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds
	narrow	broad	latest	year ago		latest	year ago	
Australia	- 1.3	+12.3 Jun	5.05	4.82	5.19	5.86	5.49	7.05
Britain	+ 9.6	+ 6.5 Jun	3.97	4.91	3.93	4.62	4.81	5.79
Canada	+17.2	+ 7.2 Jul	2.99	3.82	3.50	5.12	5.36	6.96
Denmark	+ 3.2	+ 7.3 Jun	3.60	4.67	4.00	4.80	5.02	6.84
Japan	+30.6	+ 3.3 Jul	0.02	0.03	-0.01	1.21	1.35	1.28
Sweden	+ 2.2	+ 4.2 Jun	4.18	4.27	4.57	5.06	5.07	5.08
Switzerland	+10.9	+ 5.8 Jul	0.75	3.21	1.27	3.02	3.28	4.03
United States	+ 5.2	+ 7.4 Jul	1.72	3.38	2.16	4.19	4.85	6.56
Euro area†	+ 7.6	+ 7.1 Jul	3.37	4.27	3.57	4.52	4.74	5.42

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.93%, Japan No.241 1.24%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.002%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholm Börsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Stockmarkets

Market indices

	Aug 28th	2002		% change on		
		high	low	one week	record high	Dec 31st 2001 in local currency in \$ terms
Australia (All Ordinaries)	3,090.4	3,440.0	2,937.8	- 0.8	-10.2	- 8.0 - 0.9
Austria (ATX)	1,123.2	1,357.2	1,113.5	nil	-35.3	- 1.5 + 8.6
Belgium (Bel 20)	2,290.6	2,899.8	2,001.6	+ 1.7	-37.8	-17.7 - 9.3
Britain (FTSE 100)	4,274.0	5,323.8	3,777.1	- 2.1	-38.3	-18.1 -13.5
Canada (Toronto Composite)	6,579.9	7,958.1	6,161.1	- 1.3	-42.2	-14.4 -12.5
Denmark (KBX)	189.7	233.4	169.0	+ 0.3	-37.1	-15.6 - 6.8
France (SBF 250)	2,298.9	3,081.9	2,067.7	- 1.3	-47.6	-22.9 -15.0
(CAC 40)	3,419.7	4,688.0	3,023.7	- 1.9	-50.6	-26.1 -18.5
Germany (Xetra DAX)	3,682.8	5,462.6	3,332.7	- 4.8	-54.3	-28.6 -21.3
Italy (BCI)	1,213.0	1,513.0	1,077.8	- 0.8	-44.4	-15.4 - 6.7
Japan (Nikkei 225)	9,766.7	11,979.9	9,420.9	+ 1.3	-74.9	- 7.4 + 2.6
(Topix)	953.9	1,139.4	922.5	+ 0.7	-66.9	- 7.6 + 2.4
Netherlands (AEX)	377.4	531.2	318.5	- 0.9	-46.2	-25.5 -17.9
Spain (Madrid SE)	671.6	848.1	625.9	- 0.7	-41.4	-18.5 -10.2
Sweden (Affarsvarlden Gen)	154.8	236.8	143.1	- 1.4	-61.3	-33.1 -24.6
Switzerland (Swiss Market)	5,265.9	6,694.1	4,607.8	- 4.0	-37.4	-17.9 - 9.2
United States (DJIA)	8,694.1	10,635.3	7,702.3	- 2.9	-25.8	-13.2 -13.2
(S&P 500)	917.9	1,172.5	797.7	- 3.4	-39.9	-20.1 -20.1
(Nasdaq Comp)	1,314.4	2,059.4	1,206.0	- 6.7	-74.0	-32.6 -32.6
Europe (FTSE Eurotop 300)*	962.8	1,279.7	862.3	- 2.2	-43.5	-23.7 -15.9
Euro area (FTSE Ebloc 100)*	815.1	1,125.1	732.5	- 2.3	-47.4	-26.7 -19.2
World (MSCI)†	835.1	1,024.4	756.7	- 2.5	-42.4	na -16.8
World bond market (Salomon)‡	495.2	499.8	430.3	+ 0.4	- 0.9	na +12.6

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in \$ terms.

The Economist commodity price index 1995=100

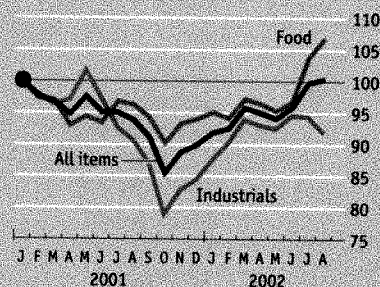
	Aug 20th	Aug 27th*	% change on	
			one month	one year
Dollar index				
All items	72.7	73.2	+ 2.4	+ 7.1
Food	75.9	77.1	+ 3.9	+12.0
Industrials				
All	68.3	68.0	+ 0.1	+ 0.3
Nfa†	71.7	71.0	+ 1.4	+ 5.6
Metals	65.5	65.5	- 1.1	- 4.0
Sterling index				
All items	75.2	75.5	+ 5.1	+ 1.4
Euro index				
All items	98.0	98.3	+ 3.1	- 0.6
Yen index				
All items	92.1	92.1	+ 0.7	+ 4.9
Gold				
\$ per oz	308.50	310.85	+ 1.7	+14.2
West Texas Intermediate				
\$ per barrel	29.82	28.83	+ 5.4	+ 5.9

* Provisional. † Non-food agriculturals.

Commodity prices

The Economist all-items, dollar-based commodity index has rallied by 18% from an 18-year low in October. Since mid-May the food index has risen by 14%, thanks to stronger cocoa and grain prices. But prices for industrial commodities have slumped; the metals index has fallen by 7% since July.

\$ terms, Jan 2001=100



Source: The Economist

Trade, exchange rates and budgets

Trade balance*, \$bn latest 12 months			Current account				Exchange rate		Currency units					Budget balance % of GDP 2002†
			\$bn latest 12 mths	The Economist poll % of GDP, forecast 2002 2003		trade-weighted†		per \$		per £	per euro	per ¥100		
						Aug 28th	year ago	Aug 28th	year ago					
Australia	- 0.1	Jun	- 11.6	Q2	- 3.4	- 3.4	73.5	72.8	1.81	1.89	2.79	1.78	1.53	0.1
Austria	- 2.0	May	- 1.3	Jun	- 1.9	- 1.7	na	100.4	1.02	1.10	1.57	-	0.86	-0.3
Belgium	+ 15.1	Jun	+ 13.0	Dec	+ 4.8	+ 4.9	na	99.2	1.02	1.10	1.57	-	0.86	nil
Britain	- 45.6	Jun	- 31.2	Q1	- 2.0	- 1.9	105.0	105.3	0.65	0.69	-	0.64	0.55	-0.8
Canada	+ 34.0	Jun	+ 14.7	Q1	+ 2.4	+ 2.5	76.2	77.6	1.56	1.54	2.40	1.53	1.32	1.0
Denmark	+ 7.2	Jun	+ 3.5	Jun	+ 1.7	+ 1.7	103.0	102.7	7.57	8.18	11.6	7.42	6.39	2.2
France	+ 9.0	Jun	+ 28.4	Jun	+ 1.7	+ 1.6	na	101.9	1.02	1.10	1.57	-	0.86	-2.0
Germany	+100.6	Jun	+ 27.2	Jun	+ 1.2	+ 1.1	na	98.9	1.02	1.10	1.57	-	0.86	-2.8
Italy	+ 9.3	May	- 2.9	May	nil	nil	na	72.7	1.02	1.10	1.57	-	0.86	-1.4
Japan	+ 80.6	Jun	+107.0	Jun	+ 2.8	+ 2.8	136.9	140.0	118	120	182	116	-	-8.0
Netherlands	+ 23.7	Jun	+ 2.7	Q2	+ 4.0	+ 4.2	na	98.2	1.02	1.10	1.57	-	0.86	0.1
Spain	- 36.9	May	- 16.5	May	- 2.1	- 1.8	na	74.4	1.02	1.10	1.57	-	0.86	-0.3
Sweden	+ 14.7	Jul	+ 8.3	Jun	+ 3.3	+ 3.4	77.5	74.3	9.31	10.4	14.3	9.13	7.86	2.1
Switzerland	+ 3.0	Jul	+ 25.7	Q1	+ 9.8	+10.1	113.7	108.9	1.50	1.67	2.31	1.47	1.27	na
United States	-435.5	Jun	-398.1	Q1	- 4.4	- 4.7	113.1	117.0	-	-	1.54	0.98	0.85	-1.0
Euro area	+ 79.2	Jun	+ 24.8	Jun	+ 0.4	+ 0.5	81.7	79.4	1.02	1.10	1.57	-	0.86	-1.5

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast.

Overview

Venezuela's GDP fell by 9.9% in the year to the second quarter. The collapse was due in large part to OPEC's decision to cut oil production, which accounts for a quarter of Venezuelan output. Venezuela's \$11 billion current-account surplus of a year ago dwindled to \$1.9 billion in the year to the second quarter.

The devalued *real* helped **Brazil** to narrow its current-account deficit to \$550m in July, its smallest since January 1997. Brazil's 12-month deficit is running at some \$16.7 billion, down from \$27.1 billion a year ago. Brazil's stockmarket index rose by 10.0%.

Corruption

Finland is reckoned to be the least corrupt country in the world, according to the annual index of perceptions of corruption compiled by Transparency International, a Berlin-based organisation that aims to fight corruption worldwide. The index focuses on the misuse of public office for private gain. France is thought to be more corrupt than Botswana, and Argentina almost as corrupt as Russia. Perceptions of Russia are, however, improving: last year, it was as corrupt as Pakistan but now it is only as corrupt as India.

10=least corrupt



Source: Transparency International

Economy

	% change on year ago			Latest 12 months, \$bn		Foreign reserves* \$bn, latest
	GDP	Industrial production	Consumer prices	Trade balance	Current account	
China	+ 8.0 Q2	+12.8 Jul	- 0.9 Jul	+28.3 Jul	+17.4 2001	241.9 May
Hong Kong	- 0.9 Q1	-11.6 Q1	- 3.4 Jul	- 8.2 Jul	+14.1 Q1	112.3 Jul
India	+ 6.4 Q1	+ 4.0 Jun	+ 4.2 Jun	- 5.4 Jun	+ 1.4 Q1	56.5 Jul
Indonesia	+ 3.5 Q2	- 9.4 Q4	+10.1 Jul	+27.5 Jun	+ 8.4 Q3	28.4 Jun
Malaysia	+ 3.8 Q2	+ 4.9 Jun	+ 2.1 Jul	+13.4 Jun	+ 7.0 Q1	32.4 Jun
Philippines	+ 3.8 Q1	+ 5.9 Jun	+ 2.6 Jul	+ 2.6 Jun	+ 6.2 May	13.5 Jul
Singapore	+ 3.9 Q2	+17.8 Jul	- 0.4 Jul	+ 6.4 Jul	+17.5 Q2	80.3 Jul
South Korea	+ 6.3 Q2	+ 8.9 Jul	+ 2.1 Jul	+ 9.0 Jul	+ 5.3 Jul	115.4 Jul
Taiwan	+ 3.0 Q2	+11.4 Jul	+ 0.4 Jul	+18.6 Jul	+24.8 Q2	155.3 Jul
Thailand	+ 3.9 Q1	+ 6.2 Jun	+ 0.1 Jul	+ 3.8 Jun	+ 6.6 Jun	36.0 Jun
Argentina	-16.3 Q1	-12.4 Jun	+32.9 Jul	+12.6 Jun	nil Q1	9.6 Jun
Brazil	- 0.7 Q1	+ 0.7 Jun	+ 7.5 Jul	+ 6.4 Jul	-16.7 Jul	41.9 Jun
Chile	+ 1.7 Q2	- 2.0 Jun	+ 2.6 Jul	+ 2.7 Jul	- 0.6 Q2	15.1 Jun
Colombia	+ 0.5 Q1	- 0.7 May	+ 6.2 Jul	+ 0.5 Jun	- 1.4 Q1	10.6 Jul
Mexico	+ 2.1 Q2	- 0.7 Jun	+ 5.5 Jul	- 9.1 Jul	-17.1 Q1	45.5 Jun
Peru	+ 3.6 Jun	+ 2.8 May	nil Jul	+ 0.2 Jun	- 1.0 Q2	8.7 Jun
Venezuela	- 9.9 Q2	-17.1 Jun	+22.0 Jul	+ 8.0 Q1	+ 1.9 Q2	6.7 May
Egypt	+ 4.9 2001†	+ 7.8 2001†	+ 2.8 May	- 8.2 Apr	- 0.1 Q1	12.7 Apr
Israel	- 1.7 Q2	+ 1.6 Jun	+ 6.9 Jul	- 6.3 Jul	- 2.3 Q1	22.8 Jul
South Africa	+ 2.2 Q2	- 0.1 Jun	+10.6 Jul	+ 3.5 Jun	- 0.1 Q1	5.9 Jun
Turkey	+ 2.3 Q1	+ 6.6 Jun	+41.3 Jul	-10.3 Jun	+ 2.0 May	22.3 Jun
Czech Republic	+ 2.5 Q2	+ 1.3 Jun	+ 0.6 Jul	- 2.5 Jun	- 2.4 Q1	21.4 Jul
Hungary	+ 2.9 Q1	+ 4.1 Jun	+ 4.6 Jul	- 2.3 Jun	- 1.9 Jun	10.3 Jul
Poland	+ 0.5 Q1	+ 6.0 Jul	+ 1.3 Jul	-10.6 Jun	- 6.6 Jun	27.1 Jul
Russia	+ 3.7 Q1	+ 7.8 Jul	+14.9 Jul	+42.4 Jun	+28.3 Q2	39.6 Jul

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Financial markets

	Currency units			Interest rates short-term % p.a.	Stockmarkets Aug 28th	% change on		
	per \$		per £			Dec 31st 2001		
	Aug 28th	year ago	Aug 28th			one week	in local currency	in \$ terms
China	8.28	8.28	12.7	na	1,750.1	+ 0.2	+ 2.2	+ 2.2
Hong Kong	7.80	7.80	12.0	1.75	10,130.3	- 2.6	- 11.1	- 11.1
India	48.5	47.1	74.5	5.80	3,099.4	+ 0.5	- 5.0	- 5.4
Indonesia	8,886	9,150	13,656	14.87	443.0	- 3.1	+ 13.0	+ 32.2
Malaysia	3.80	3.80	5.84	3.20	724.7	- 0.8	+ 4.1	+ 4.1
Philippines	51.9	51.2	79.8	7.19	1,109.1	+ 0.4	- 5.0	- 5.6
Singapore	1.75	1.75	2.69	0.94	1,504.9	- 1.9	- 7.3	- 2.1
South Korea	1,199	1,277	1,842	4.80	724.1	- 2.8	+ 4.4	+ 14.4
Taiwan	34.2	34.6	52.5	2.10	4,789.6	- 2.0	- 13.7	- 11.6
Thailand	42.2	44.2	64.9	2.00	365.1	- 1.9	+ 20.2	+ 25.9
Argentina	3.61	1.00	5.55	64.30	376.9	- 2.1	+ 27.6	- 64.7
Brazil	3.12	2.55	4.79	17.83	10,379.9	+10.0	- 23.5	- 43.4
Chile	713	656	1,095	2.76	4,942.1	- 0.9	- 8.4	- 15.0
Colombia	2,693	2,298	4,139	7.82	1,189.8	- 0.7	+ 11.1	- 6.0
Mexico	9.89	9.15	15.2	6.69	6,115.6	- 2.4	- 4.0	- 11.0
Peru	3.61	3.48	5.55	2.72	1,190.1	- 0.5	+ 1.3	- 3.5
Venezuela	1,412	737	2,170	29.62	6,928.8	+ 3.0	+ 5.5	- 43.4
Egypt	4.60	4.26	7.07	7.15	5,261.8	+ 0.0	- 0.2	- 0.7
Israel	4.67	4.25	7.17	6.40	368.1	+ 0.4	- 17.6	- 22.1
South Africa	10.6	8.33	16.3	12.60	9,709.3	+ 0.3	- 7.0	+ 5.3
Turkey	1,630,000	1,378,000	2,504,984	42.00	9,394.6	- 2.4	- 31.8	- 39.2
Czech Republic	31.3	37.7	48.0	3.05	454.3	- 1.1	+ 15.1	+ 31.0
Hungary	250	278	385	9.81	7,696.4	+ 4.9	+ 7.9	+ 18.5
Poland	4.15	4.24	6.38	8.44	13,480.1	+ 1.2	- 3.2	- 7.8
Russia	31.6	29.4	48.6	21.00	347.5 [†]	- 0.8	+ 38.5	+ 33.6
EMF (MSCI)*	1.00	1.00	1.54	na	298.0	- 1.4	na	- 6.1
EMBI+ [†]	1.00	1.00	1.54	na	206.0	+ 1.6	na	+ 2.8

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In \$ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; UBS Warburg; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; Russian Economic Trends.

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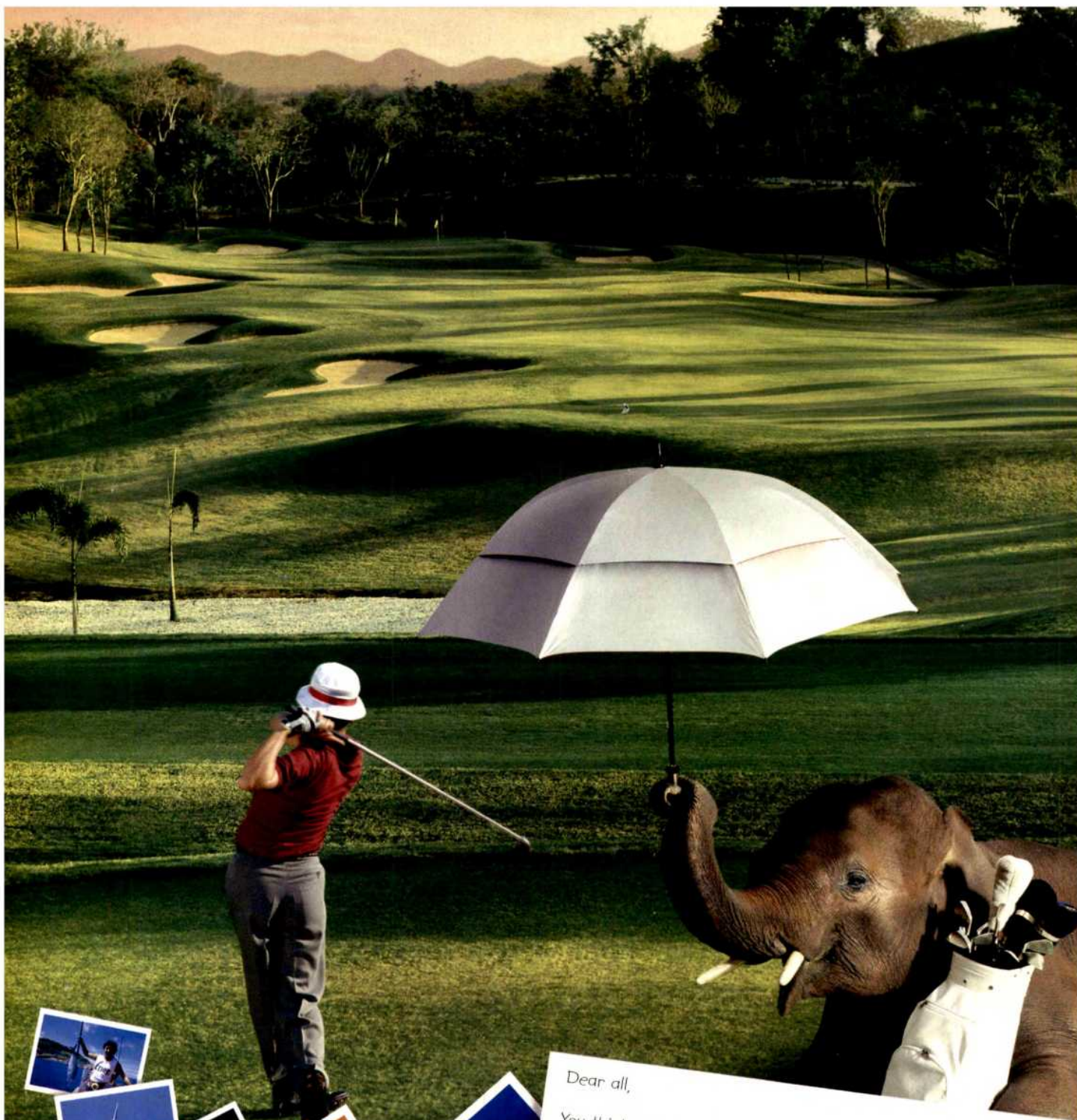
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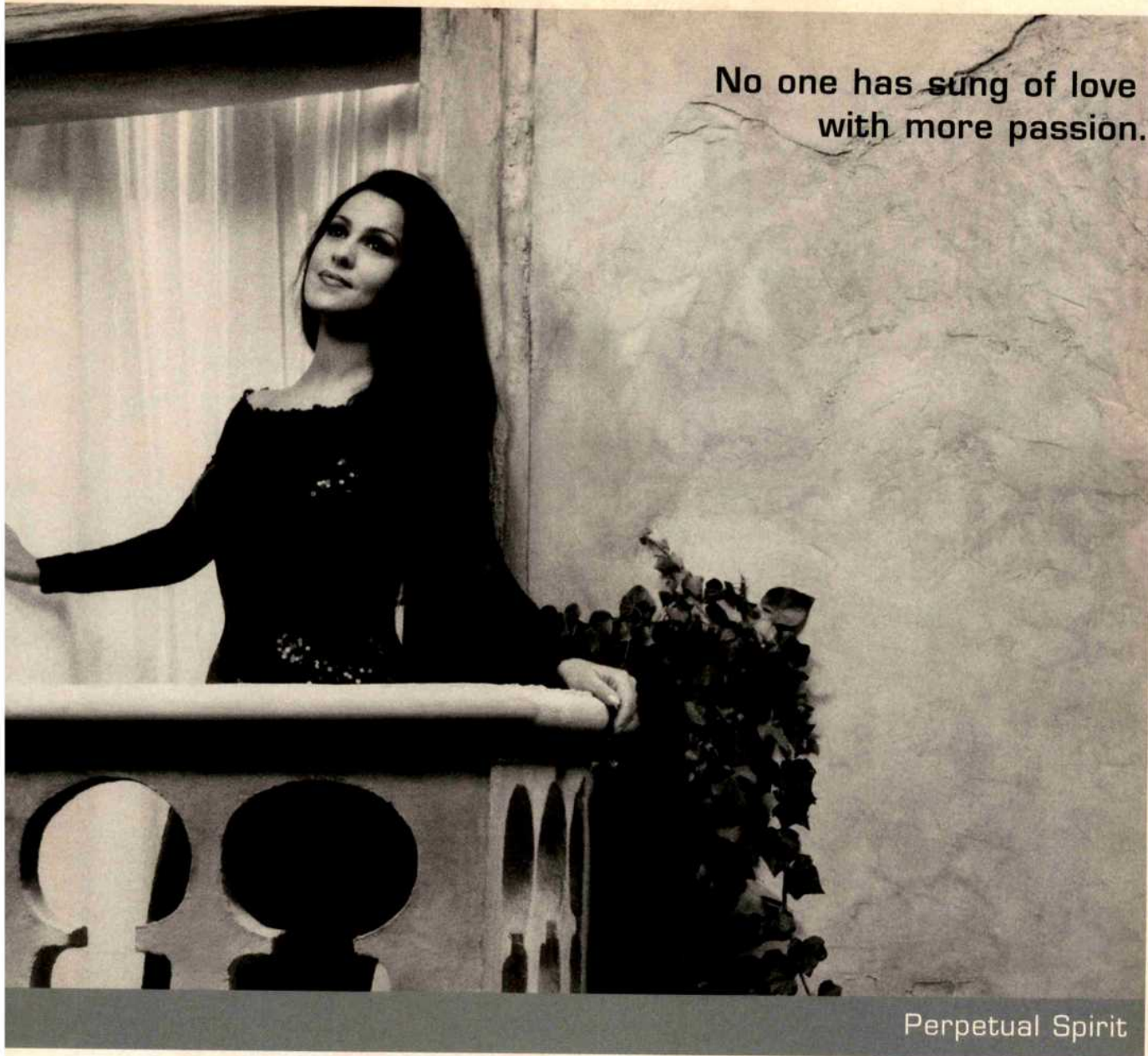
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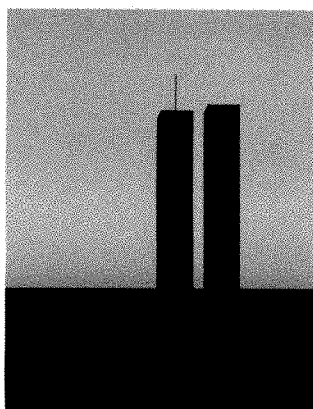


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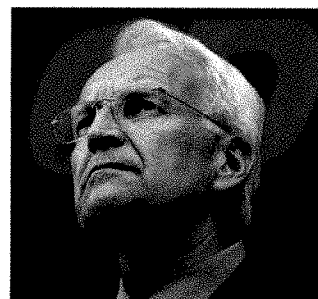
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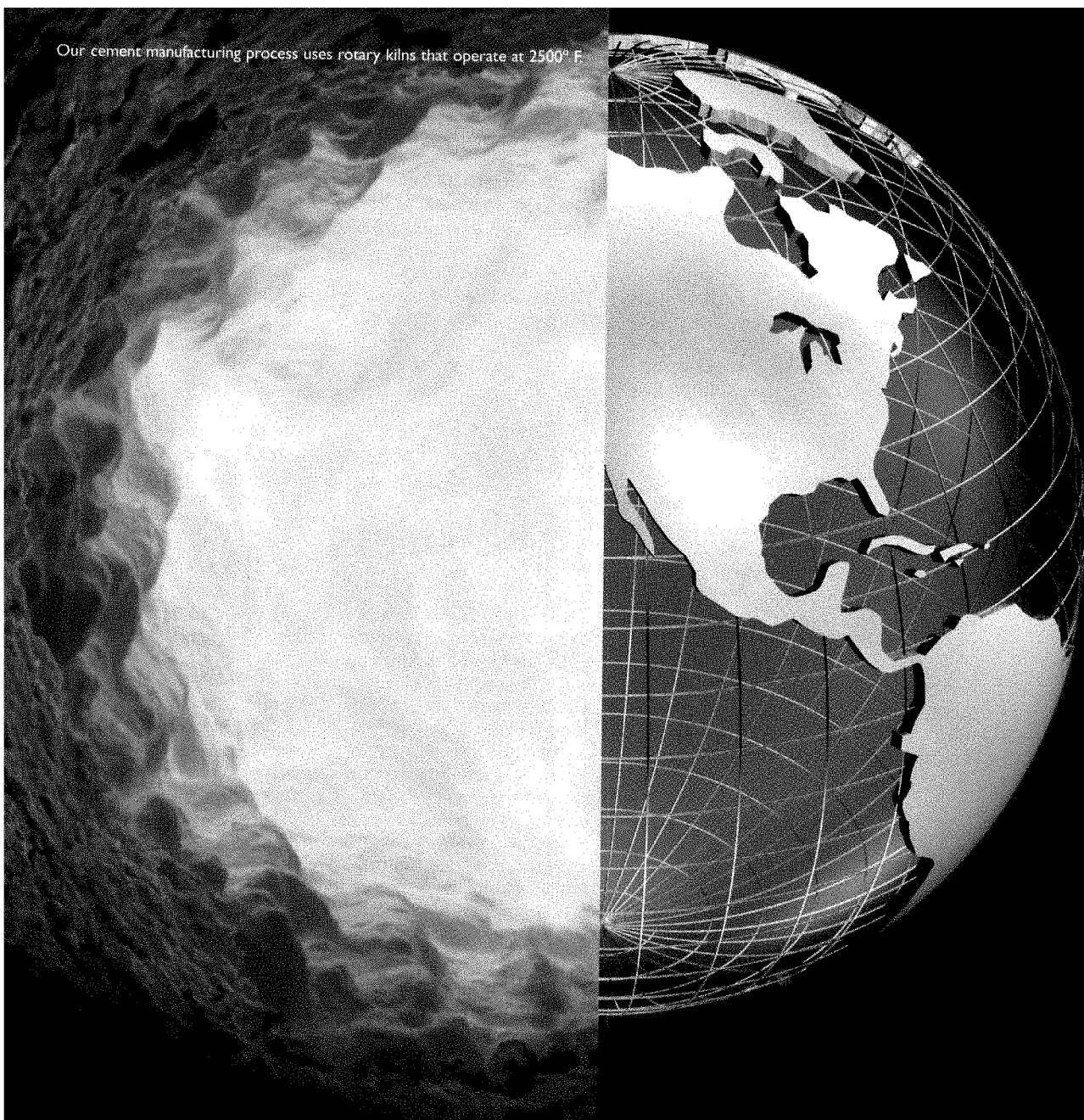
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Politics

Tariq Aziz, Iraq's deputy prime minister, told Kofi Annan, the UN's secretary-general, that Iraq was prepared to readmit UN weapons inspectors but only as part of a comprehensive settlement that would include the end of sanctions and America's threatened war. America dismissed the offer out of hand.



Arab League foreign ministers meeting in Cairo repeated their **categorical rejection** of an American assault on Iraq.

President George Bush told congressional leaders that he will spell out his **Iraq strategy** to the world when he addresses the UN next week. The issue, he said, is not inspectors but disarmament. He also pledged to consult Congress before taking action.

A survey of over 9,000 Europeans and Americans found that most would **support military action** against Iraq, but only as a joint allied attack with UN approval.

Collateral damage

Israel's defence minister called for an army inquiry into the spate of killings of **Palestinian civilians** in the past week. Some 15 civilians have been killed, including several children. Two Palestinian siblings, alleged to have helped their brother (who has since been killed) in his terrorist activities, were forcibly deported from the West Bank to Gaza after Israel's Supreme Court rejected their appeal.

Palestinian radical groups, including the al-Aqsa Brigades, rejected a call from the

new Palestinian interior minister to replace armed action with peaceful forms of resistance against occupation. Israeli police said they thwarted a massive car-bomb attack on September 5th.

The government of **Sudan** suspended peace talks with rebels of the Sudan People's Liberation Army (SPLA), blaming the rebels for continuing to fight during negotiations. The SPLA accused the government of doing the same thing.

The **Johannesburg summit** on sustainable development ended with mixed results. Targets and a timetable were reached for improving water and sanitation. But the United States prevented a target being set for boosting renewable energy. Colin Powell, America's secretary of state, was booed.

Sam Nujoma, Namibia's president and a friend of Robert Mugabe, said that **Zimbabwe's** current problems had been created by Britain. Mr Mugabe himself rebuked Tony Blair, Britain's prime minister, telling him: "Let me keep my Zimbabwe."



Ravaged by drought, **Ethiopia** appealed for food aid and other assistance. The World Food Programme estimates that nearly 6m Ethiopians are dangerously hungry.

No-frills hijacker?

A **Swedish man** of Tunisian origin was arrested in Stockholm after attempting to board a British-bound Ryanair jet with a loaded gun. The man, who had taken flying lessons in the United States, was apparently planning to attend an Islamic conference in Birmingham. He is suspected of planning a hijack.

A report from the Bosnian Serb government suggested that Muslims may have "imagined or fabricated" the **Srebrenica massacre** and concluded that up to 2,500 Muslims, mostly combatants, were killed when Serbs overran the UN safe area in 1995. The UN and Red Cross say that over 7,000 civilians died.



The government of **Gibraltar** announced a referendum on November 7th to decide on whether there should be shared sovereignty over the territory with Spain, in an effort to pre-empt British plans for a vote on an agreement with Spain over the Rock's future. Britain said it would not recognise the referendum, which is unlikely to favour any Spanish involvement in Gibraltar's future.

Shaky policies

The IMF said that "major issues" needed to be resolved before **Argentina** could hope for a loan agreement. An IMF mission arrived in the country to assess the government's economic policies, which are under attack by Congress, the central bank and the Supreme Court.

In **Guatemala**, a court began hearing charges against three army officers accused of ordering the murder of an anthropologist in 1990. It is the first time that senior military figures have faced trial for crimes committed during the country's 36-year civil war.

In **Peru**, a retired army general and former interior minister was found dead in prison after apparently committing suicide. He was an important witness in the trials for corruption of Vladimiro Montesinos, a jailed former chief of intelligence.

nos, a jailed former chief of intelligence.

Not me, governor

Andrew Cuomo announced that he was withdrawing from the race for the **New York governorship**, leaving the Democratic nomination open to Carl McCall, the state comptroller and the first black nominee. The Republican incumbent, George Pataki, is still favourite to win.

A row began about the structure of the new **Department of Homeland Security**, which involves merging 22 existing agencies. Democrats claim Mr Bush is getting rid of existing deals on union membership and workers' rights. The president talked about the need for flexibility.

A report by New York city's comptroller estimated that **September 11th** would cost the city \$83 billion-95 billion, depending on how many jobs are permanently moved out of the city.

Afghan troubles

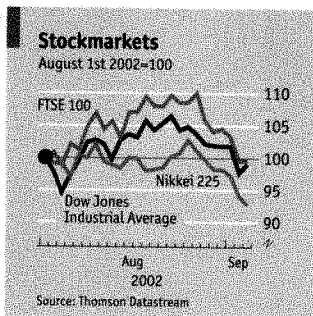
President Karzai of **Afghanistan** survived an assassination attempt when two shots were fired at his car in Kandahar. But many died when a car-bomb exploded in Kabul, the worst attack in the Afghan capital since the overthrow of the Taliban last year.



Sri Lanka unbanned the Tamil Tigers, a prelude to peace talks due to start on September 16th in Thailand.

An **Indonesian** court sentenced Akbar Tandjung, the parliamentary speaker and leader of the formerly ruling Golkar party, to three years in prison for misusing \$4.5m of state funds.

Business



World stockmarkets shuddered. The Dow Jones Industrial Average fell by 4% in a day as nerves showed in the run-up to the anniversary of the September 11th attacks, fears mounted of a war with Iraq and a report suggested that American manufacturing growth in August was flat. Markets around the world followed suit. Japan's Nikkei 225 hit a 19-year low and European bourses slipped.

American **car sales** surged by 13.5% in August, with General Motors reporting a rise of 18% on a year ago and Daimler-Chrysler one of 24% for its Chrysler arm. But the boom was largely caused by zero-interest financing offers, so it is unlikely to last.

Modus Vivendi

Vivendi Universal began the task of putting right its ill-poor results, crashing shares and a debt mountain—by flogging assets. It will sell its 50% stake in Vizzavi, a European Internet portal, to Vodafone, its joint-venture partner, for €143m (\$142m) and a clutch of publishing interests to a French publisher, Socpresse, for €330m.

Vodafone was also reported to be close to making an offer for **SFR**, a French mobile-phone company controlled by cash-strapped **Vivendi**. The British mobile company already owns 32% of SFR and could offer as much as £8 billion (\$12.5 billion) for the rest.

Bertelsmann, another media company in retreat, is pulling back from its e-commerce activities. **Amazon** was said to

be interested in its closest rival, **BOL**, Bertelsmann's on-line book and music operation. Bertelsmann also failed in its bid for **Napster**, a no longer operational Internet music-swapping service. An American court blocked the takeover after opposition from the rest of the music industry.

Reports suggested that a study commissioned by **France Telecom** of **MobilCom** cast doubts on the long-term prospects for the German mobile-phone company. The report may help France Telecom, which owns 28.5% of the German mobile company, to make a choice between abandoning MobilCom to bankruptcy or launching a bid for full ownership.

United at the top

UAL, United Airlines' parent company, appointed Glenn Tilton, an executive at ChevronTexaco, to the jobs of chairman, chief executive and president. An early task may be deciding which of his three hats to wear if the loss-making airline files for bankruptcy.

Reports surfaced that **Martha Stewart Living** was planning to replace Martha Stewart (the person) as its chief executive. Ms Stewart is under investiga-

tion over alleged insider trading, which has caused shares in her eponymous company to collapse. The disentanglement of person from brand may prove hard for both.

A Pennsylvania judge granted a temporary injunction against the planned sale of **Hershey Foods** by the trust that owns most of its shares. But the trust will appeal against the ruling.

Switzerland's **Roche** sold its vitamins division to **DSM**, a Dutch specialty-chemicals company for €2.2 billion (\$2.2 billion). Profitability in vitamins has suffered since the European Commission broke up an international price-fixing cartel in which Roche was a leading figure. Roche will retain liability for any fresh claims arising from the case.

ABB, a Swiss-Swedish engineering group, said that it would sell its finance arm to America's **GE Commercial Finance** for \$2.3 billion. ABB will use the cash to cut its substantial debt mountain.

Fallen Citigroup

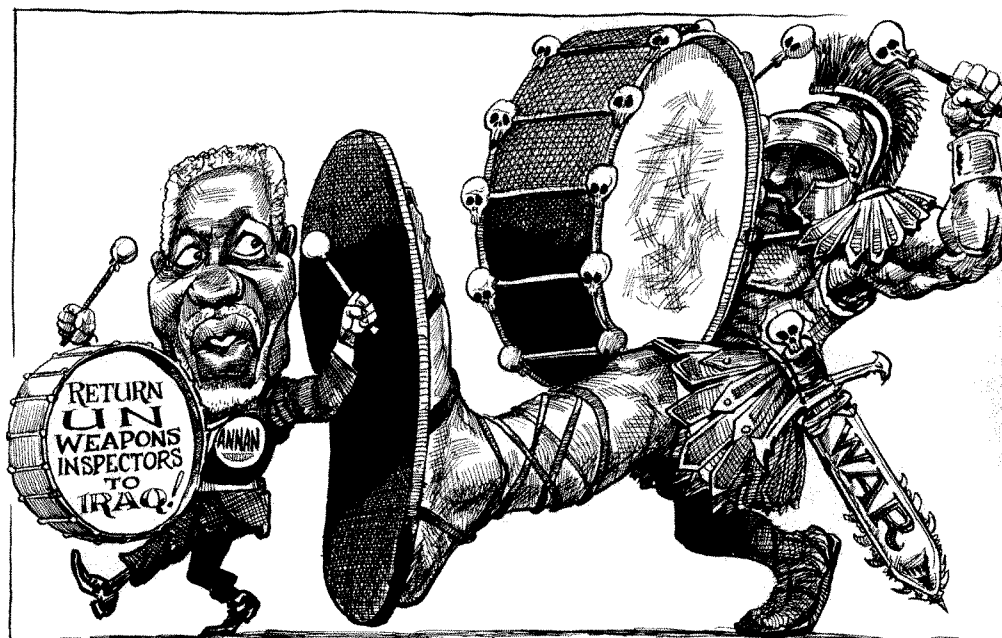
Shares in Wall Street's leading banks suffered; **Citigroup** led the way. Its shares fell by 10% as fears mounted over poten-

tial liabilities at the world's biggest financial-services conglomerate. Problems include congressional investigations into its role in the Enron and WorldCom affairs, and a widening of regulatory probes into allocations of initial public offerings by a subsidiary, Salomon Smith Barney. The IPO practices of other banks are also under scrutiny.

Zurich Financial, Europe's third-biggest insurer, reported a loss of \$2 billion for its first half. It confirmed plans to shed 4,500 jobs, over 6% of the total, and to make a rights issue of \$2 billion-2.5 billion. The troubled insurer replaced its chief executive earlier this year.

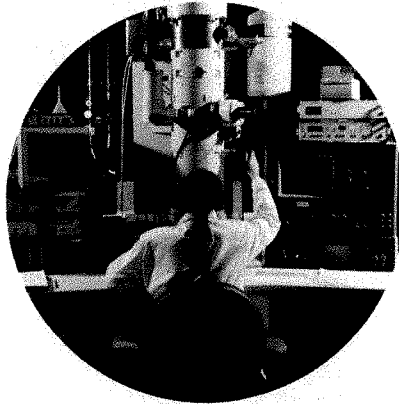
The president, chairman and two other top executives resigned from **Mitsui**, a Japanese trading house, after taking responsibility for bribes allegedly made by the company to a Mongolian official involved in a power-generator contract. Days before, the president and chairman of **Tokyo Electric Power** resigned over cover-ups of faked safety reports on the company's nuclear reactors.

Other economic data and news can be found on pages 96-98



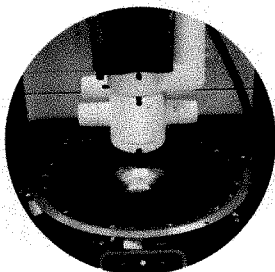
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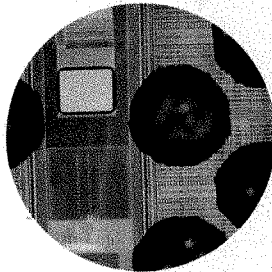


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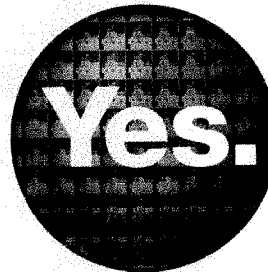
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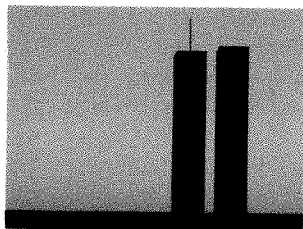
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Remember

September 11th changed the world. But not enough



IT IS a terrible memory. A memory of four plane-loads of people, setting off on a beautiful morning but then hijacked to their deaths. A memory of thousands of innocent, unsuspecting civilians, of many nationalities, slaughtered when three planes hit the twin towers of the World Trade Centre and one side of the Pentagon; and of many more, lucky to survive but living ever since with the nightmare of that day, one year ago. It is a memory, also, of how the world looked a moment before 8.48am on September 11th 2001, and of how, by the end of that day, the world was different.

A year later, much more has changed, and mostly for the better. An America that Osama bin Laden and his al-Qaeda terrorists wanted to frighten, proving that the world's greatest power was actually weak, vulnerable and cowardly, has shown a remarkable resolve. Its patient but determined use of military power in Afghanistan, and threat of it in Iraq, has created more fears of its strength than contempt for its weakness. Afghanistan was liberated from the Taliban, al-Qaeda's bases and forces there were destroyed or scattered, and that war-torn country managed to choose its own provisional government. An astonishingly broad alliance backed America in that war, and the two old superpower foes—Russia and China—were respectively supportive and acquiescent.

Some of the successes lie in what has not happened rather than what has. America has not turned in on itself, seeking to hide from a hostile world: rather, its international engagement has been reinvigorated, even if its tolerance of opposition or of compromise in that engagement has diminished. The process of globalisation has not been put into reverse, either by the demands of security or by a disenchantment with open markets: if anything, the chances of a new round of trade liberalisation have increased, despite a weak world economy. And, most important of all, if Mr bin Laden and his sort hoped that their atrocities, and the American military response to them, would bring to life a mass movement in the Islamic world, they have so far been sorely disappointed. Not in Pakistan, not in Saudi Arabia, not in Egypt, not in Palestine, not in Indonesia, not even in Afghanistan itself have the numbers fighting, or even marching, against America ever gone beyond a few thousand at a time. Moreover, there has been no big terrorist success since September 11th, although several attempts appear to have been thwarted.

That is where, for all the success, the memory becomes important again. In at least one vital respect the world has not changed in the past year. This is that the sort of extremists who carried out the slaughter on September 11th could do so again. Their operations have been disrupted, their hopes may have been disappointed. But last year's attacks took just a handful of people, with a handful of money, using low-technology methods. The ability of police and intelligence services, in America but also elsewhere, to stop them has improved, but not to such a degree as to provide a true sense of security. Any-

one who believes the risks are small should think back to September 10th last year, when the risks also looked small; and should then ask themselves whether the attitudes and perceived grievances that persuaded 19 well-educated men to kill themselves and thousands of civilians have meanwhile changed or gone away.

The dangers of the status quo

It is nigh on impossible for normal people to put themselves into the minds of the sort who planned or carried out last year's slaughter, which makes it also hard to be sure whether others are now more, or less, likely to do something similar. A few things are clear, however. One is that, although no mass anti-American movement has emerged, there are still plenty of extremists in the Islamic, but especially the Arab, world. Another is that the march of technology is making it easier all the time for such groups to plan atrocities but also to use the ghastliest weapons. Third, and perhaps most important, is the fact that all the possible sources of anti-American anger, justified or not, remain intact: bases in the Saudi holy lands; sanctions and "no-fly" zones for Iraq; bloody conflict in the Middle East, with American support for Israel; and repressive, alienating Arab regimes, especially in Egypt and Saudi Arabia, that are thought to enjoy America's backing.

In the past year, the biggest changes have come in America and in Central Asia, both in Afghanistan and in the surrounding countries (see pages 23 and 26). Now, and for the coming year, the main debate is over whether the next wave of change will or should come in the Arab world, begun with a "regime change" in Iraq but not ending there (see pages 28 and 38). Or whether to attack Saddam Hussein would be to take an unnecessary risk, damaging in its own right but also destabilising for the rest of the Arab world. Or, in the end, over whether there is any link between the memory of September 11th 2001 and the danger of Mr Hussein and his chemical, biological and nuclear weapons.

For the past few months, this debate has become frenzied but incoherent. The great virtue shown since September 11th by America in general, and President George Bush in particular—that patient determination—has become a vice on this issue. The more time that goes by without a clear decision from him on what America will do, in Iraq itself but also with regard to the United Nations, the more that a vacuum has been created into which has rushed confusion, rumours of divisions within the administration or between America and its supposed allies—and Iraqi ministers seeking to sow even more confusion and division.

Now, at long last, an effort seems to be under way to create coherence—or, at least, to provide a coherent decision about which to argue. This weekend, Britain's prime minister, Tony Blair, is to fly to President Bush's official retreat, Camp David, for talks about Iraq; Mr Bush says he also plans phone conversations with the leaders of France, China and Russia, the other three permanent members of the UN Security Council; and on September 12th Mr Bush is due to address the UN General Assembly, which gives him a fine opportunity to present ►

► his plans, his arguments and some of his evidence.

Much of that effort at persuasion, and much of the debate about it, will centre on Saddam Hussein. So it should: the Iraqi dictator's violation of international agreements, his efforts to obtain weapons of mass destruction, his willingness to use them against his own people and his neighbours, his declared territorial ambitions, all make him a dangerous man who needs at last to be removed from power. But as that effort, and the debate, proceeds, the memory of September 11th needs also to be kept firmly in mind. The events of that day showed what unscrupulous, murderous people can achieve. But they also showed how dangerous is the status quo in the Arab world in general, of which Iraq is but a part.

If terrorist attacks by groups such as al-Qaeda are to be made less likely in future, that status quo needs to be changed,

in numerous ways. Those ways do begin with Iraq, for the current policy of containment through debilitating sanctions and bombing raids from bases in the Gulf is not sustainable. They also, though, begin in Israel and Palestine, where a parallel effort needs to be made to create circumstances in which the two states can live securely side by side. And they move on to the Arab countries themselves, where at the very least the blame for those nations' economic and social failures needs to be pinned on the local regimes, not on outside powers, which are forced by history or convenience to support them.

In the coming months, probably the most seductive argument that will be deployed against a war in Iraq will be the idea that it would threaten the Arab world's stability. Yet it is that very stability—or, rather, sterility—that created al-Qaeda, its supposed grievances, and September 11th. Remember. ■

Japan and North Korea

Koizumi's gambit

Coaxing North Korea in from the cold



JAPAN'S Junichiro Koizumi may be about to discover, like others have before him, that it is easier to make history with prickly North Korea than it is to make progress. On September 17th, he plans to become the first ever Japanese leader to call on its exclusive boss, Kim Jong Il. He has a lot to talk about: the Japanese citizens abducted by North Korean agents over the years, the rockets that now have all of Japan in their firing range, and the nuclear and other ambitions that make North Korea a founder-member of George Bush's "axis of evil". His North Korean host, meanwhile, demands \$10 billion or more in compensation for Japan's past colonial rule. Might the planned Koizumi-Kim talks nonetheless signal a thaw in the North's frost-bitten relations with Japan, South Korea and America? Or will history repeat itself—as farce, or worse?

Two years ago, South Korea's President Kim Dae-jung made his own "historic" journey north, proffering generous dollops of aid and investment for North Korea's clapped-out economy. He returned with promises that his northern namesake would pay a return visit to the South, that divided families would be allowed to meet, that economic contacts would flourish, allowing the first official breaches (a road and rail-freight link were mooted) in the cold war's final frontier. A few families have been briefly reunited, at a price. But it turned out that the northern Mr Kim wanted only to shore up his own communist-cum-feudal regime. He swiftly retreated behind a wall of hostility, pocketing all the cash and goodies he could.

Will he behave better this time? There are some encouraging signs. He has launched a round of economic reforms—"perfecting communism", his officials insist—though it is unclear whether as a prelude to a wider economic opening, or simply in a desperate effort to stave off ruin (the flow of North Korean escapees—another 15 or so sought asylum at diplomatic premises in China this week—steadily increases). Yet it is South Korea, Japan and the United States that Mr Kim has to deal with if he wants to end his pariah status and draw in the

investment needed to rebuild decrepit roads and factories. Economic talks with South Korea did resume last month. Hoping to be struck off America's list of states that sponsor terrorism—and thus become eligible for help from the likes of the IMF—North Korea has signed some UN anti-terrorism conventions, and may be about to hand over four ageing Japanese terrorists it had been harbouring.

In the light of all this, America and South Korea have lent Mr Koizumi their support. But if he is to advance the cause of peace on the peninsula, there are some pitfalls to be avoided.

History in the making

The summit was Mr Koizumi's idea, boosting his sagging ratings at home, so he is under pressure not to return empty-handed. But nothing could be better than something, if the something he is offered is a deal that would breach the common front that Japan, South Korea and America have achieved in facing down the threat from North Korea.

The North has tried wedge-driving before. It attempted to talk South Korea into supplying it with vast amounts of electricity. But that would have enabled it to wriggle out of a deal it struck with America in 1994 to abandon its production of bomb-making plutonium in return for two nuclear-power reactors and supplies of oil. Before the nuclear components of the reactors arrive, North Korea must come clean to international inspectors about its past nuclear activity. Loth to do so, it may yet hope to coax enough aid from Japan to give it the wriggle room it needs to keep the inspectors at bay.

In fact North Korea already receives food aid for its half-starved people. Mr Koizumi's message should be that more aid and better relations can be had, not just from Japan but from South Korea and America too, but in return for verifiable steps to reduce the danger North Korea poses all round—from its missiles, from its missile sales to unstable parts of the world, from its nuclear-, chemical- and biological-weapons dabbling, and from the array of troops and guns dug in just across the border from the South Korean capital, Seoul. If Mr Koizumi's visit were to kick off wider talks on a deal of that sort, he could indeed claim to be making history—not faking it. ■

Sri Lanka

Talking with Tigers

The best chance for peace in two decades



THE Tamil Tigers, one of the world's most vicious terrorist organisations, were unbanned on September 4th by the Sri Lankan government that has spent the past 19 years fighting them. To many Sri Lankans, especially those whose relatives have been killed in suicide attacks and bombings, or driven out of their homes in the north and east of the island, legitimising the Tigers will seem like an obscenity. To many Tiger foot-soldiers, the prospect of negotiations, due to begin at the Thai resort of Sattahip on September 16th, yielding anything less than the full independence they have fought for will seem like a sell-out. But in the interests of ending a war that has crippled an otherwise beautiful and bounteous country, both sides will have to make some difficult sacrifices.

Talking to terrorists is never palatable. But the government has been unable to defeat the Tigers militarily, despite emptying its own treasury in the attempt. Though treated with respect rather than love by the Tamil population of Sri Lanka, the Tigers are broadly supported and assisted by them. Only they, after all, have been able to advance the case for greater rights for the Tamils—a minority in the island as a whole, but a majority in the north-east. In such circumstances, an accommodation is the only realistic alternative to an endless and costly war. Whether that amounts to rewarding terrorism depends on what happens next.

Concessions from the government side will have to be matched by similar wisdom on the part of the Tigers' leadership. It is impossible to know what the Tigers' bottom line is, but there is some reason to hope that they do now recognise

that their main demand, for an independent state in the north-east, will never be acceptable to Sri Lanka's government. Such a constitutional change would need to be approved by the Sri Lankan parliament. There is no prospect of this happening, because of the strength of Sinhalese nationalist parties in the parliament chamber.

Autonomy but not independence

Nor should it. It is far from clear that the north-east of Sri Lanka meets the tests required for statehood. At least until the Sinhalese were driven out over the last ten years or so, the areas, with the exception of the Jaffna peninsula, were shared by Tamils, Sinhalese and Muslims, and the Muslims, who still remain there, have no desire to see themselves abandoned to a Tamil state. Historically, too, there is no convincing case for such a creation. What there are, however, are legitimate grievances on the Tamils' side. Independent Sri Lanka has treated the Tamils badly, most notoriously in the 1972 constitution, which proclaimed Sinhala to be the official language.

Fortunately, there are signs of flexibility from the Tigers' leader, Velupillai Prabhakaran. His goal of a Tamil "Eelam", or homeland, might, he has suggested, be met by something less than an independent state, and more like an autonomous region. That still raises the fear that any such area might become merely a fief for Mr Prabhakaran and his henchmen. But there is some reason to hope otherwise. In the absence of a peace deal, moderate Tamil parties have felt they have no option but to accept the Tigers' leadership. Once an accommodation is reached, different Tamil voices will have a chance to be heard. Sri Lanka has had many false dawns, and deals have been struck before over this issue, only to unravel. But there is much to play for in Sattahip. ■

The Johannesburg summit

Small is all right

Was the sustainable-development summit a wash-out?



"FOURTEEN hours to help save the world." So screamed a headline in Britain's *Guardian* newspaper earlier this week. Such agitation reflected the sentiments of many of the lobby groups at the UN summit on sustainable development,

which concluded on September 4th. But now the summit is over, and those crucial final hours were spent, apparently, to no great effect. The planet is presumably doomed.

Either that, or the *Guardian's* headline and many others like it were idiotic. That in fact would be our guess.

If the world had needed saving, it would have been wrong to expect an event such as the UN summit to rise to that chal-

lenge in the first place. Happily, though, the world does not need saving. On most measures, both human welfare and the environment are getting better, not worse. Particular problems, such as AIDS and climate change, do need more attention and international co-operation. When it comes to curbing poverty, on the other hand, international co-operation is not the main thing that is needed. In any case, it is ludicrous to suggest that the earth is in grave peril.

The right criterion for assessing Johannesburg is the progress made on a narrow set of issues that fall at the intersection of poverty and the environment: water, energy, fisheries and farming. Here, the summiteers actually achieved a modest success (see page 73).

Despite resistance from the European Union, the final declaration includes a promise to phase out farm subsidies. There ►►

is no way to enforce this undertaking—but still it may prove useful in shaming countries such as France when they next obstruct farm reform. The same goes for a promise to restore the world's ailing fisheries.

More encouraging still is that such humdrum topics as septic systems and cow-dung fires rose to the top of the agenda. The reason is that unsafe water and sanitation, and dirty energy use, make up the leading preventable causes of death in the developing world. The summit agreed to a firm timetable and target for improving water and sanitation. It also agreed to tackle "energy poverty", while rejecting a firm target for boosting renewable energy.

It might seem odd to have set a target for water and sanitation but not for energy—but this was probably right. Digging boreholes or building lavatories pose no great technological challenges: political will is the real barrier to progress on these issues. Energy poverty, in contrast, is more difficult. The technology is evolving rapidly. Forcing expensive, complicated and soon-to-be-outdated methods on poor villagers has little to recommend it.

It would be far better to stop governments from rigging energy markets in ways that encourage waste and pollution

while holding back the poor. Many rich countries subsidise domestic fossil fuels and the export of power plants which use those fuels. Poor countries often subsidise grid electricity for their urban elites—leaving less power and money to help the poor in the countryside. The summit may not have tackled these failings head-on, but it did agree to intelligent language on phasing out "environmentally harmful" subsidies.

In praise of non-government opportunities

The summit also marked a shift in the role that agencies other than governments—be they green groups, charities aiming to relieve poverty, or big business—can play. Dozens of new partnerships were launched to tackle specific local problems, and hundreds of existing ones were examined and discussed. This marketplace of ideas and experiment is the nitty-gritty of sustainable development. UN officials even announced that they were ready to bypass governments and directly finance firms that offer employees treatment for AIDS.

The prominence of business led many to complain that the summit was hijacked by "free-market ideology". If only. As the litany of ongoing subsidies for pollution and squandered resources makes clear, there was never any danger of that. ■

America's monetary policy

Greenspan's bubble bath

If the Fed had popped America's bubble sooner, its economy would be healthier



SINCE early 1998 *The Economist* has repeatedly argued that the Federal Reserve should have tightened policy sooner to let some air out of America's economic and financial bubble. This view won us few friends in America; most commentators even denied that it was a bubble. Yet most now agree that it was perhaps the biggest financial bubble in American history. It has also been the biggest bust, with almost \$7 trillion knocked off share values since early 2000—more, as a share of GDP, than after the 1929 crash. As the imbalances created by this bubble continue to hold back America's economy, more people are starting to point the finger of blame at the Fed.

Such criticism last week provoked Alan Greenspan, the Fed's chairman, to defend his record (see page 72). Mr Greenspan argued that central banks cannot use interest rates to prick bubbles in their early stages because they can never be sure if there is a bubble or not. Moreover, he said, interest rates are a crude weapon. A rise in rates sufficient to prick a bubble could push the economy into recession.

Dealing with bubbles is devilishly difficult, but Mr Greenspan overstates his case. Uncertainty should not mean inaction: central banks do not shy from stamping out inflation just because they are unsure about the size of the output gap. And if by pricking a bubble a central bank causes a recession, that may still be better than the alternative of letting financial imbalances worsen, raising the spectre of a much deeper recession when the bubble eventually does burst. The longer the party continues, in short, the worse the eventual hangover.

The job of a central bank is not just to prevent inflation, but

also to ward off threats to economic and financial stability. Central banks should not set targets for asset prices. But a sharp rise in share prices accompanied by a big increase in borrowing should set alarm bells ringing. Heavy borrowing leaves firms and individuals dangerously exposed: when asset prices collapse, the nominal value of their debts remains fixed, creating severe balance-sheet problems for households and firms—as Japan has painfully discovered since 1990.

It would have been better if the Fed had raised interest rates earlier in the late 1990s to head off America's stockmarket boom. Yet its mistake was understandable, because central banks do not have a mandate to prick asset-price bubbles. The awkward truth is that bubbles are popular. The public regards high inflation in the prices of goods and services as a bad thing, but rising property and share prices as good things. Central banks' independence goes only so far. If the Fed had raised interest rates when inflation was low and succeeded in pushing down the stockmarket, thereby trimming the wealth of the 50% of Americans who own shares, Congress might have been tempted to curb the Fed's power. No wonder central bankers prefer to let bubbles pop in their own good time. But if, as a result of its bubble bursting, America now suffers several years of sluggish growth, or worse, they may think again.

A less forgivable mistake was that Mr Greenspan acted as something of a cheerleader for the "new economy". Even if some of the increase in productivity growth was real, his enthusiasm contributed to investors' euphoria. They seized on all of his comments to justify their bullishness about future profits. Ironically, Mr Greenspan was among the first to give warning of a bubble in 1996, drawing attention to the market's "irrational exuberance". What a pity he failed to put America's monetary policy where his mouth (briefly) was. ■



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£250,000 - £999,999	4.00%	3.85%	3.80%
£1,000,000 +	4.10%	3.95%	3.90%

¹The Annual Equivalent Rate (AER) is a notional rate quoted for interest bearing accounts which illustrates the contractual (gross) interest rate, as if paid on an annual basis. The actual return for US Dollar and euro accounts will be slightly higher since, by convention, interest is calculated on a 360 day year basis. All rates are subject to change without prior notice.

HONG KONG

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3201 Dah Sing Financial Centre, 108 Gloucester Road,
Wanchai, Hong Kong.

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A fertile subject

SIR – You fail to suggest the most obvious reason for America's recent fertility increase ("A tale of two bellies", August 24th). American economic life has become far less secure over the past 25 years, and more than anything else changes to economic security are associated with changes in national fertility rates. Numerous studies and observations uphold the hypothesis that fertility rates are negatively related to increases in financial and economic security.

What does this say about American capitalism? Increased fertility rates will exacerbate the problem of public investments, especially in children, as reflected in our worsening capacity to create much of our own human capital in schools. If living standards rise in nations that typically supply us with market-ready human capital, our ability to attract this subsidy to GDP growth could fall. We may then suffer flat or falling growth per head that would take decades to reverse.

DALTON GARIS
City University of New York
New York

SIR – While Europeans are far from perfect in the environmental sphere, at least we are trying to deal with our mountains of consumer waste and tackle other green issues. The average American is by far the most profligate user of natural resources in the world and the biggest emitter of most pollutants. Without a drastic alteration to lifestyles, the prospect of another 200m Americans bodes ill for our suffering planet.

STEPHEN PSALLIDAS
Newcastle

SIR – You miss one exception to Europe's falling fertility. France is enjoying un *mini* baby boom. It is now fashionable for couples to have three or four children. Some of the reasons are puzzling. Many are not: wonderful kindergartens, financial aid for families, amenable school timetables and shorter working weeks

that help women to keep their jobs and raise children at the same time.

CHRISTIAN GERONDEAU
Paris

SIR – Remarkably, Americans are having more children despite the absence of the generous maternity leave that is the norm in Europe and the rest of the industrialised world. Why? America may not be a convenient place to have children but it is a great place to raise them.

ADRIAN NG'ASI
KELLY CURRAN
Silver Spring, Maryland

SIR – Much of the reason for fertility levels in America can be gleaned from Lexington on the growth of religious fundamentalism (August 24th). The fertility trend correlates with the rise of the "teach abstinence only" approach to sex education in American schools. Increased funding and support from the Bush administration means that more of America's young are denied medically accurate sex education. This sad fact stands in the way of efforts to reduce teenage pregnancy. A younger age structure is both good and bad, and being a "mistake" in your parents' eyes does not doom you to failure but it is hard to see it as a helpful start.

SARA SEIMS
President and CEO
Alan Guttmacher Institute
New York

Apocalypse, soon?

SIR – Lexington's views on millenarianism in America lack psychological, historical and maybe even geographical perspective (August 24th). The "In case of Rapture, this car will be driverless" bumper stickers were a fad that was hardly limited to north Florida and simply meant "I'm holier than thou" – not exactly a new sentiment. The "Left Behind" series is popular entertainment. The biblical references resonate especially strongly in middle-America with its high proportion of Christians but readers no more constitute a

cult than fans of other science fiction, and probably less so than fans of Star Trek.

As far as millenarianism in politics goes, both Pat Robertson, a former presidential candidate, and James Watt, a former interior secretary, believed that the end is nigh. Mr Robertson was sure his children would see it if he did not. Mr Watt's beliefs implied that conservation of natural resources was not merely useless but actually wicked as God had provided exactly the right amount of coal, oil, etc, and it was an offence not to use it. Many people believe in some general way that the world will end in chaos but they still want their Social Security benefits. Any politician who hopes to survive will put that concern over the apocalyptic horrors of Revelation.

WALTER READ
Fresno, California

The Czech past

SIR – There are several legacies of the Benes decrees that leave room for concern; to raise them is hardly populism ("A spectre over Central Europe", August 17th). If we rightly condemn ethnic cleansing in Bosnia in 1992, then how can it have been acceptable in 1945? If the issue is, as you say, a matter of "ancient wrongs" then why is this not applied to the Holocaust? Does a state have the right to declare a group to be no longer a part of its demos simply because it is ethnically different? Can a democratic state like the Czech Republic ever live at ease with Germany and Austria unless it comes to terms with the undemocratic acts committed in 1945?

GEORGE SCHÖPFLIN
London

Stem cells in Singapore

SIR – You allege that Singapore's main draw for top scientists is our "permissive climate for research" and that no country has gone further in its guidelines for stem-cell research ("Send in the clones"

August 24th). This is inaccurate. Singapore's government has accepted recommendations by Singapore's national Bioethics Advisory Committee (BAC) on human stem-cell research. These were made after an extensive survey of current practices in the leading jurisdictions and after consultations with religious and community groups in Singapore. The recommendations incorporate good precedents practised in other countries and are not more liberal than, for example, those prevailing in Britain.

In accepting BAC's recommendations, the government intends to enact legislation where all human stem-cell research conducted in Singapore will have to be approved, licensed and closely monitored by the Ministry of Health. Singapore's approach is to ensure that the human benefits of stem-cell research could be derived without compromising ethical standards.

KAREN TAN
Press secretary to the minister for health
Singapore

Urgent business proposal

SIR – You tell us to beware of e-mails that promise riches ("Scam of scams", August 24th). I receive a great many – all from relatives or business associates of deceased African rebels or dictators. It is nice to be singled out for my "honesty and integrity" so often but my usual response is to forward the e-mail to "abuse@" followed by the domain name of the sender. Of course, there is a fantastic way to turn the tables on these rascals and so profit from their greed. I will be happy to provide details of this scheme to each reader who sends me \$50.

MIKE CONRAD
London ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James's Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com



CHIEF EXECUTIVE

London

CDC Capital Partners owned by the UK Government is a leading risk capital investor in developing economies. With over 50 years' experience and a dedicated team of investment professionals, CDC's mandate, set by its shareholder, is:

- To maximise the creation and long-term growth of viable private sector businesses in developing countries, especially poorer countries.
- To achieve attractive rates of returns which will mobilise third party capital flows into developing countries.
- To implement social, environmental and ethical best practice.

In 1999, CDC became a public limited company. It trades as CDC Capital Partners. CDC is in the process of organising its activities through a series of specialist funds, targeted principally at private equity and mezzanine investment in South Asia and Africa, as well as the power sector and small to medium enterprises throughout the emerging world.

It is anticipated that a new fund management company will be separated from ownership of the capital to manage existing and future funds of CDC. When appropriate, this management company will be a majority owned by the private sector.

A Chief Executive for this company is sought. The ideal candidate will require genuinely imaginative leadership – embracing business and financial strategy; people management and organisational culture; and relations with private sector investors, partners, development institutions and governments worldwide.

Candidates are likely to be internationally experienced chief executives or board-level directors, with a proven track record which demonstrates commercial success and exceptional leadership of people. Relevant experience within private equity, emerging markets and capital raising will be very helpful.

For further information, please visit CDC's website at www.cdcgroup.com which includes CDC's relevant sector and geographical experience, as well as pertinent financial and corporate information.

To express your interest, please send a full CV, covering letter and current remuneration details to Douglas Board at Saxton Bampfylde Hever plc (reference DFAD/E), PO Box 198, Guildford, Surrey GU1 4FH, UK.

Fax +44 1483 531 882. Email: DFAD@SAXBAM.CO.UK to arrive **not later than 20th September 2002**.



ADVERTISED RECRUITMENT AND CONSULTANCY
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UK Competition Commission

Senior Economist

£55,000 to £60,000

and possibly more for an exceptional candidate

Do you enjoy using economics to understand the nature of competition between firms? Would you like to have an impact on real decisions, affecting competition, prices and the behaviour of firms? We are looking for a strong economist to join the senior management team at the Competition Commission, and work with the Chief Economist to deliver the changes stimulated by the 2001 Competition White Paper.

Competition Commission economists play the core role of providing advice and analysis to the members of the Commission on whether firms are behaving in an anti-competitive fashion. The Senior Economist is responsible for managing the work of 5 to 10 economists, working largely on inquiries.

To join us you will need to demonstrate:

- a strong track record as a professional economist
- a relevant background and keen interest in competition economics – ideally with at least five years experience in micro-economics and industrial economics, and preferably some special knowledge of competition policy issues
- evidence of being a good manager
- the ability to influence senior decision makers, and explain complex economic issues to non-economists

In return we can offer a fascinating range of work on inquiries at the cutting edge of competition policy, plus a package that includes a generous leave allowance and a first class pension scheme. We are based in Central London.

Further details about the job can be obtained from our website: www.competition-commission.org.uk or from Amanda Rowlett, the Chief Economist on 020 7271 0217.

To apply please send a c.v. with a covering letter explaining why you are applying and outlining how your skills and achievements relate to the job requirements, to Ian Smith at ian.smith@competition-commission.gsi.gov.uk. The closing date is 27 September 2002.

The Competition Commission is committed to appointments being made on merit and to a policy of equal opportunities. Applications are welcome from all qualified individuals regardless of race, ethnic or national origin, religion, marital status, disability or sexual orientation.

UNITED NATIONS
NATIONS UNIESFRAMEWORK CONVENTION ON CLIMATE CHANGE - Secretariat
CONVENTION - CADRE SUR LES CHANGEMENTS CLIMATIQUES - Secrétariat

The United Nations Framework Convention on Climate Change (UNFCCC) is the focus of the political process to address Climate Change. The Convention secretariat is supporting the Convention and its Protocol by a range of activities, including substantive and organizational support to meetings of the Parties. The secretariat is seeking to fill the following position:

**Deputy Coordinator (D-1)
Methods, Inventories and Science Programme
(Post Number: FCB-13002-C-D-1-001)**

Main responsibilities

The successful candidate will serve as the Deputy Coordinator of the programme and is responsible for planning, coordinating and implementing the Methods subprogramme. He/she provides leadership in identifying methods and developing guidelines related to estimating greenhouse gas emissions from sources, projecting greenhouse gas emissions, evaluating the effects of measures and assessing impacts of climate change. He/she serves as an alternate member of the management committee of the UNFCCC secretariat, providing technical, policy and management support to the programme Coordinator on all matters.

Qualifications and experience

- Advanced university degree in technical, natural, environmental science or a related discipline.
- Extensive experience developing and managing national and international climate change programmes and policies, particularly relating to climate change science, methods and compilation of greenhouse gas inventories.
- At least twelve years experience, of which four should have been in an international environment.
- Excellent command of written and spoken English. Working knowledge of other United Nations languages desirable.

Competencies

- Communicate ideas effectively in writing and orally.
- Manage, lead and motivate teams in a multicultural environment.
- Work effectively with multiple state leaders from national governments, scientific organisations and non-governmental organisations.

Remuneration

The post is based in Bonn, Germany and is at the D-1 level (indicative annual net salary: US\$81,366 with dependents and US\$75,209 without dependents), plus post adjustment and international benefits package.

To apply

- For more details please refer to the vacancy announcement on our web site: unfccc.int
- Deadline for applications 26 September 2002. Expected date for entry on duty as soon as possible.
- Quoting Vacancy Number 02/E026, address a detailed Curriculum Vitae in English or preferably complete and submit a United Nations Personal History Form (P-11), available on our website to:

Chief, Human Resources Unit

United Nations Climate Change Secretariat (UNFCCC),
P.O. Box 260 124, D-53153, Bonn, Germany.

Fax: 49-228-815-1999, e-mail: vacancies@unfccc.int

Please note that only candidates under serious consideration and contacted for an interview will receive written notice of the selection process.



**INTERNATIONAL FUND FOR
AGRICULTURAL DEVELOPMENT (IFAD)**

Via del Serafico No. 107, 00142 Rome, Italy
Fax: +39 06 5043463, E-Mail: vacancy@ifad.org

DIRECTOR, POLICY DIVISION, EXTERNAL AFFAIRS DEPARTMENT

IFAD is an international financial institution and a specialized UN agency focusing on rural development and agriculture. With an annual work program of around USD 500 million of loans and grants, IFAD operates in 115 developing countries targeting the poor in the rural areas through programmes and projects. IFAD's mission is to enable the rural poor to overcome their poverty. The overall strategic objectives of the Organization are to (i) Strengthen the capacity of the rural poor and their organizations, (ii) Improve equitable access to productive natural resources and technology, and (iii) Increase access to financial services and markets. The focus of the organization is to achieve maximum sustainable impact for the rural poor. This is mainly achieved through direct field operations within the country programs and through policy dialogue and advocacy at the international, regional and national level.

Duties and responsibilities at the D-1 level:

IFAD has recently established a new Policy Division. The Director will be responsible for developing, organizing and managing the division. The Policy Division will have a key role in translating IFAD's field experience into policies such as IFAD's contribution to the development community. The Director will manage the integration of work across the Organization and establish processes and channels for policy development and advocacy. The Director will have a key role in managing IFAD's policy advocacy activities. This includes development of partnerships with external stakeholders in the international development community to ensure that IFAD is well connected and positioned in the system. It also implies relating and taking part in ongoing international policy work and debating and channeling new ideas and thinking back into IFAD's policy work. The Director will manage the staff members of the division, diverse in nationality and gender, and provide leadership, support, coaching and feedback to motivate staff and maximize their potential.

Specific responsibilities

- Provide leadership for policy development within IFAD;
- Develop, present and manage the division's annual program of work and budget within the overall objectives of the organization;
- Day-to-day management of the staff members of the division e.g. mentoring, provide performance feedback, provide feedback on individual work programs, support staff career development, etc.;
- Build up routines and procedures for the new policy division to facilitate policy development and advocacy;
- Establish networks and working groups inside and outside IFAD to improve sharing of experience and knowledge and development of policy;
- Manage administrative requirements of the division that pertain to assigned staff or tasks;
- Accountable for the output and results of the division.

Qualifications and experience:

- Proven track record of management, in particular policy management, capabilities essential;
- Demonstrated strong leadership ability in a multicultural setting and the ability to accomplish work through motivating people and encouraging team work;
- Extensive experience and knowledge about rural development and agriculture. Proven ability to lead and develop policy in a managerial position. Experience in working within the international development community;
- Excellent written and oral communication skills;
- University degree in a relevant discipline such as economics, agricultural economics or social anthropology, followed by international experience in development work with a sound understanding of socio-economic policy and partnership issues with a strong poverty reduction focus;
- High level of initiative and ability to work under limited supervision and under pressure;
- Ability to plan, organize and prioritize work;
- Fluency in English essential. Knowledge of French, Spanish or Arabic desirable.

Please forward your application in duplicate to Personnel Division no later than 06 October 2002. For more details please visit our web-site at www.ifad.org. Please note that any application received by IFAD after the deadline will not be considered.

Due to the number of applications anticipated, only short-listed candidates will receive an acknowledgement. Applications from women candidates are particularly encouraged.

ECONOMIST/BUSINESS - SURVEY SPECIALIST

The World Bank, the leading multilateral organization in global economic and financial development, is currently seeking an **Economist/Business-Survey Specialist** for its Foreign Investment Advisory Service (FIAS). The position is for a two year appointment based in the Bank's headquarters in Washington, DC.

The Foreign Investment Advisory Service (FIAS) is a joint facility of the International Finance Corporation and the World Bank. The mandate of FIAS is to provide advice to client governments in developing/transition countries who want to attract more and better-quality foreign direct investment.

Responsibilities: design/adapt a range of business-survey instruments for policy analysis; establish standards for FIAS surveys and supervise FIAS survey work; supervise and/or conduct FIAS project-specific survey work; and supervise refinement and update of a data base for survey results.

Required Skills: Masters or PhD in economics and/or statistics required; minimum 8-10 years' experience in economic analysis/statistics in developing/transition countries, including 5 years experience in designing, implementing, and analyzing business surveys; good oral and written communication skills; and the ability to work with and intellectually lead others. Language skills (Arabic, Chinese, French, Russian, Spanish) in addition to English preferred.

The World Bank offers an internationally competitive compensation package. Interested candidates can access the detailed job description and apply on-line through the World Bank's career web site at: www.worldbank.org or fax their application to (202) 522-0198 (but not both). The closing deadline is Friday, September 20, 2002. Women and nationals of developing countries are strongly encouraged to apply. Due to the expected volume of applications, only short-listed candidates will receive responses.



**The
World Bank**



International Water and Sanitation Centre

International Water and Sanitation Centre IRC is an independent non-profit-organization, working as an international knowledge centre in the field of drinking water supply, sanitation and related environmental issues in developing countries. The focus of IRC is on: 1) providing improved access to and promoting the use of knowledge among sector institutions and stakeholders 2) building capacity of Knowledge Centres for the Water and Environmental Sanitation (W&ES) sector in developing countries and countries in transition. IRC's ambitions are to be:

- A leading knowledge broker in the W&ES sector, with an accessible client responsive multilingual knowledge base
- A leading low cost publishing and dissemination house for the W&ES sector
- A leading facilitator of Resource Centres in developing nations

IRC is a professional organization with some 40 dedicated staff and a network of partners in (mainly) developing countries. IRC is presently finalizing an internal reorganization process and is investigating the possibilities for cooperation/integration with the proposed UNESCO-IHE institute in Delft, a move which would allow IRC to reach out to a much wider user group. To guide IRC's activities and to realize its ambitions, IRC is currently seeking an inspiring and innovative director.

The new director will guide the development of the vision of IRC in its political, scientific, international and social context and translates this into strategic options and strategies for their implementation. She/he will have a clear vision of the future positioning of the institute

and our partner institutes in an international environment. She/he will be able to create opportunities for IRC, will support improvements in IRC's work, and will develop and maintain an international network of contacts. The new director will be an inspiring personality, motivating and stimulating staff to work as an effective interdisciplinary team.

Requirements

- Minimum academic degree at masters level
- Relevant professional experience of at least 15 years, with experience in developing countries, of which preferable at least 5 years in short or long term assignments abroad
- Proven general management experience at strategic organizational level
- Fluent in English, preferably fluent in Dutch and one other language (French, Spanish, Portuguese)
- Preferably a working permit in the European Union

DIRECTOR

IRC's offer

You will be offered a working week of 36 hours, a competitive annual salary depending on qualifications and experience, and good employee benefits including training opportunities.

Interested candidates are kindly requested to respond with a full CV and cover letter:

**Twynstra Gudde Management
Recruitment attn. Martin Planthof,
PO Box 907, 3800 AX
Amersfoort, the Netherlands.**
You can also send your letter and CV by email to mpn@tg.nl.

For additional information please visit IRC's website at <http://www.irc.nl>

Twynstra Gudde



Gas and Electricity Markets Authority
NON-EXECUTIVE MEMBER

£15k (2-3 days a month)

London

The Secretary of State for Trade and Industry wishes to appoint a seventh non-executive member with particular understanding of environmental issues to the Authority, which is the statutory body responsible for the work of OFGEM. Under the Utilities Act 2000, Ofgem is the independent regulator of the UK's gas and electricity markets. These industries contribute some £13bn to UK GDP and provide essential services for domestic, industrial and commercial customers. They also have major environmental impact.

The primary duty of the Authority, which is chaired by Callum McCarthy, is to look after the interests of consumers, present and future, wherever practicable through promoting competition, and every member of the Authority must work towards this end. The Authority is also required to have regard to broader Government policies on social and environmental issues. It is charged with ensuring security of gas and electricity supply within the framework of competitive markets.

The person appointed will have a distinguished track record in his or her own field. While their primary focus may or may

not be environmental, the individual will have gained significant breadth of experience about environmental issues and their interaction with markets and national policies. Sufficient organisational experience at a senior level to be a non-executive board member of Ofgem and ability to contribute across a range of policy and management issues are essential. Knowledge of the energy sector will be helpful but not essential.

The annual remuneration for the post will be £15,000 plus approved expenses, with appointment likely to be for 3 years in the first instance. The Authority meets about a dozen times each year, and it is estimated that a time commitment of 2-3 days each month is required.

For further information, including how to apply, please refer to our advisor's website at WWW.SAXBAM.COM/ARC or telephone +44 (0) 1233 214 529 (8am-10pm 7 days a week), in either case quoting reference DFGL/E not later than Tuesday 24 September 2002. Applications will close on Tuesday 1 October 2002.



ADVERTISED RECRUITMENT AND CONSULTANCY
 A PRACTICE WITHIN SAXTON BAMPFYLDE HEVER & CO



A new era for Irish financial services.

The Irish Financial Services Regulatory Authority (IFSRA) is being established, through the enactment of the Central Bank and Financial Services Authority of Ireland Bill, 2002, to supervise all financial institutions in Ireland. The Authority will put the best interests of consumers at the heart of financial services regulation, creating a sound financial market place and setting strong standards of business conduct. IFSRA will also ensure that Ireland continues as an attractive and soundly regulated location for the financial services industry. For the Authority to fulfil its goals as a world-class organisation, the highest levels of professionalism and expertise will be required. As a result, IFSRA is seeking to make the following key appointment:

CHIEF EXECUTIVE

You will be responsible for leading the regulation of the financial services industry in Ireland, ensuring that all financial service institutions operate soundly and fairly. As CE, you will be responsible for pulling together the different strands of regulatory practice into a single, coherent approach. The public face of IFSRA, you will build effective relationships across a broad range of industry, Government and consumer interests, ensuring that IFSRA performs to the highest international standard, with appropriate transparency and public accountability. Confidently networking at the most senior levels, you are a charismatic leader, with the stature, experience and people skills to communicate effectively with all interested parties.

You will have a third-level education, ideally in business or economics and/or an appropriate professional qualification with the ability to demonstrate in-depth management experience in a sophisticated financial services, professional services or relevant public body. Experience of financial services regulation and/or consumer protection is very desirable, and you will need a clear understanding of the economic environment in which Irish business operates. You will also need the ability to grasp the "big picture", understanding the implications and influence of strategic decisions on the future development of IFSRA. **CE/TE/02**

An appropriate remuneration package will be negotiated to attract the best candidates. If you have what it takes to play a key role in this exciting new organisation, please send full details of your career to date, quoting appropriate reference to Siobhan Frain, Amrop Hever, 33 Lower Baggot Street, Dublin 2. E-mail: ifsra@amrop.ie Closing date for receipt of applications is Friday 20th September 2002.

INTERNATIONAL CENTER FOR TRANSITIONAL JUSTICE (ICTJ)

The International Center for Transitional Justice (ICTJ) is a human rights organization based in New York City that aims to strengthen the field of transitional justice—assisting societies in transition to respond to a legacy of massive abuse—through in-country assistance, policy advice, capacity building, and strategic research. The ICTJ responds to requests for assistance and comparative information from organizations in civil society and governments. Its work focuses on strategies to document abuse, establish effective truth commissions, prosecute perpetrators, reform abusive institutions, provide reparation to victims of violence, and promote reconciliation. The ICTJ works closely with other organizations in the field in all of its program areas.

Currently, the ICTJ is offering a career opportunity to a dynamic, team-spirited, detail-oriented professional with an advanced degree in law, public policy, international affairs, or other relevant field of social science.

SENIOR ASSOCIATE

The Senior Associate will provide technical assistance, comparative information, and policy advice to organizations in civil society and governments. His or her work will include analyzing and drafting legislation, speaking in public forums on transitional justice, and offering policy analysis on lessons learned from previous transitions. The Senior Associate will participate in the ICTJ's missions abroad, and will also provide assistance from ICTJ headquarters in New York, working under the direct supervision of a Program Director.

Requires minimum four years' relevant human rights experience; a high level of professionalism; strong public speaking, communication, and interpersonal skills; computer proficiency; and the ability to work under pressure and to strict deadlines. Excellent written and spoken English essential; fluency in French strongly preferred; other languages desirable. Must be willing to travel internationally.

The ICTJ provides an excellent salary, comprehensive benefits, and a committed multicultural, international environment. The ICTJ will pay reasonable relocation expenses and will assist employees to obtain necessary U.S. work authorization.

Please send cover letter, resume, and contact information for three references by 30 September 2002 to:

Joyce Munn, Global Nonprofit Partners

Dag Hammarskjöld Station, P.O. Box 20363 DHCC, New York, NY 10017

Email: joyce.munn@att.net, Fax: 212.872.1451

The ICTJ is an equal opportunity/affirmative action employer strongly committed to hiring and retaining a diverse and internationally representative staff.

KING'S COLLEGE, CAMBRIDGE

Director of Development £48,000 (subject to review)

The Director will be expected to maintain and enhance relationships with alumni and to direct the fund raising efforts of the College. She or he will be paid a professorial salary and will be elected a Fellow of the College. Applications will be welcomed both from experienced fund-raisers and from individuals with other relevant professional experience.

Further information is available at
<http://www.kings.cam.ac.uk/vacancies/>
or from Roger Salmon, the First Bursar,
at King's College, Cambridge CB2 1ST
Telephone 01223 331217
or bursar@kings.cam.ac.uk.

UNITED NATIONS



NATIONS UNIES

ASSISTANT SECRETARY-GENERAL FOR HUMAN RESOURCES MANAGEMENT BASED IN NEW YORK

An opportunity to serve at the international level managing personnel of the United Nations and shaping reform of the system

The United Nations invites applications for its top-ranking post in human resources management. The candidate must be a leader in the field, able to meet the high expectations of Governments, capable of dealing with a large number of heads of numerous departments and other components; have in-depth knowledge of, and extensive experience in, current human resources management practices; be technologically competent to promote automation in HR systems and services; have a proven track record of having successfully led teams of diverse cultural backgrounds and implemented change management in large organizations, preferably with international experience.

The United Nations Secretariat serves 190 Member States. It has 15,000 staff members from more than 150 countries working in different parts of the world. The Assistant Secretary-General for Human Resources leads a dedicated team of some 200 HR practitioners in performing traditional human resources functions and spearheading change in that area, under the rubric of the Secretary-General's reform programme for the Organization.

Functions

- Set strategic vision and direct its implementation in complex environments.
- Lead negotiation, development and implementation of HR policies and programmes.
- Coordinate HR matters in the UN system.
- Act as principal interlocutor for the Secretary-General with staff and Member States on HR issues.

Experience and skills

- Demonstrated success in setting and realizing organizational vision and direction.
- Extensive knowledge of, and experience in, current HR management practices.
- Demonstrated ability to successfully perform change management in a large organization, preferably with international exposure.
- Demonstrated ability to lead culturally diverse teams.
- Technologically competent to promote automation in HR services and systems.

Competencies

- Vision, leadership
- Outstanding presence and communication skills
- Team and consensus builder and able to empower others
- Astute judgment and decision-making
- Persuasive, flexible and pragmatic negotiator

For further information, please visit our website at jobs.un.org.

MINISTRY OF WORKS

PRICEWATERHOUSECOOPERS

EXECUTIVE SEARCH & SELECTION

Chief Executive Tanzania National Roads Agency (TANROADS)

The Government of Tanzania decided in 2000 to transform the Roads Departments of the Ministry of Works into an Executive Agency, Tanzania National Roads Agency (TANROADS). TANROADS took over responsibility for all aspects of trunk, regional and essential feeder roads of Mainland Tanzania, subsidiary businesses and personnel management. The main functions of TANROADS are managing the maintenance and development works and operations of the network, implementing road safety and environmental measures and giving advice on the strategic framework, policies and plans for the road sector.

The Opportunity

The Ministry of Works wishes to recruit a chief executive for TANROADS who will be responsible for the day to day operations and proper management of its funds, property and personnel.

Specific duties include:

- preparation of strategic and annual business plans and reporting;
- overseeing implementation of approved strategic and business plans;
- procuring and concluding contracts;
- effective management of financial and human resources; and
- preparation of annual performance reports.

Selection Criteria

The successful candidate should be a mature and experienced individual with a post-graduate degree in Civil Engineering, Transport Economics or equivalent qualifications and training in management. He/she should have 20 years experience in the road sector with a minimum of 10 years of successful performance at a management level. Previous experience from within the Region will be an added advantage. This post is open to international competition and is to be filled as soon as possible. The successful candidate will be offered a three-year contract and a negotiable international competitive remuneration package plus a performance related bonus.

Mode of Application

If you want to accept this challenge and you meet the criteria outlined above, please apply in writing, in strict confidence, to the address below enclosing:

- an application letter showing how you meet the criteria for the post;
- a full typed curriculum vitae including current remuneration;
- copies of qualification certificates;
- full address at work/home, including phone and fax numbers where available; and
- three referees, including your current employer (who will not be contacted without your prior approval).

Send your application to reach us on or before 4:00 pm, 7th October, 2002.

Executive Search & Selection (Ref. TR), PricewaterhouseCoopers, P.O. Box 45, Dar es Salaam
Fax: 251-51-133200 E-mail: information@tz.pwcglobal.com



EUROPEAN CENTRAL BANK

The European Central Bank (ECB), established in Frankfurt am Main on 1 June 1998, is seeking to fill the vacancy detailed below in the General Economic and Financial Statistics Division of the Directorate General Statistics.

The ECB has its own terms and conditions of employment, including a competitive salary structure, retirement plan, health insurance and relocation benefits. Candidates must be nationals of a Member State of the European Union.

ECONOMIST-STATISTICIAN (Ref.: ECB/103/02/I/TE)

The main task of the Directorate General Statistics is to provide, explain and publish the statistics needed to support the policy responsibilities of the European Central Bank (ECB). For this purpose the Directorate General Statistics works closely with other areas of the ECB, as well as with the national central banks of EU Member States, the European Commission (especially Eurostat), the national statistical institutes of EU Member States, and the statistical departments of certain international institutions. Within the Directorate General Statistics, the General Economic and Financial Statistics Division is responsible for general economic statistics, financial accounts and government finance statistics.

The successful candidate will work on macroeconomic statistics, in particular external trade and external transactions in national accounts for the euro area, the EU Member States and selected countries outside the EU. He/she is expected to contribute to the design and development of the ECB internal databank on monthly external trade in values, volumes and unit values as well as quarterly and annual national accounts. These tasks require teamwork within the Directorate General Statistics and with other areas of the ECB (in particular the Directorate General Economics) and with the European Commission (in particular Eurostat). The successful candidate will be involved in preparing briefing material for members of the Executive Board and for senior management. He/she will attend European and international meetings.

Qualifications and experience

- Advanced university degree in economics, or proven ability to perform the tasks commensurate with such a formal academic qualification, together with an economic background in the macroeconomic analysis of external trade and/or external transactions in national accounts and balance of payments.
- Experience in external trade and/or current and capital accounts in balance of payments statistics. Knowledge of the European System of Accounts (ESA 95) and the IMF Balance of Payments Manual, 5th edition, would be considered an asset.
- Good knowledge of statistical methods and techniques, in particular index concepts and time series analysis.
- Experience with MS Office applications such as Word and Excel, and interest in database-oriented work. Working knowledge of FAME would be an asset.
- Ability to work under pressure as part of a highly motivated team in an international environment. Experience with international working groups would be an advantage.
- Very good command of English with proven drafting ability. A working knowledge of at least one other official Community language is required.

Applications

Applications should be submitted in English and include a covering letter, curriculum vitae and a recent photograph, together with references confirming the required experience and skills. They should be addressed, quoting the reference number, to the **European Central Bank, Recruitment and Staff Development Division, Postfach 16 03 19, 60066 Frankfurt am Main, Germany** and should reach the ECB no later than **24 September 2002**. Applications will be treated in the strictest confidence and will not be returned.

This vacancy has also been posted on the ECB's website at www.ecb.int. To meet the deadline, a copy may be sent by fax to +49 69/1344 7979 or by e-mail to recruitment@ecb.int. However, a signed application must still be sent by post.

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Night fell on a different world

WASHINGTON, DC



In three articles, we look at the "different world" (in George Bush's words) that has emerged from the terrorist attacks of September 11th 2001. We begin in America

HIGH on the buildings around One World Trade Plaza, three cameras peer into the abyss. They are recording the history of the site's rebuilding in photographs taken at five-minute intervals. Had they been there that terrible day, they would have recorded the destruction of the World Trade Centre as a more sudden vanishing than the billowing cloud the world saw.

Since then, for the past few months, the time-elapsed photographs have shown little change: a few workers move places, but the site remains empty. Strung together over coming years, however, those snapshots will show a new building being raised, like an unfolding flower in a nature film. America's history since September 11th has been a little like that: a sudden transforming moment, then a period of stasis (which continues), leading to a new construction yet to be decided.

September 11th has been a transforming event not just because of its enormity, but also because of the nature of the attacks. Fifty thousand Americans were killed in a decade of fighting in Vietnam. They were combatants, dying on battlefields. Over 3,000 people were murdered in a morning in New York, Washington and Pennsylvania. They were going about their daily lives until death came literally from a clear blue sky. Americans were no longer safe on their mainland—something that had not been true of the Vietnam, Korean or second world wars.

One of America's founding myths is that it is a place apart, a continent pro-

tected by high seas. From Thomas Jefferson's warning to the new republic against "entangling alliances", to Ronald Reagan's summons to his fellow citizens to build an ideal "city on a hill", Americans have seen their country as a safe, separate place. This made them profoundly different from Europeans who, with the exception of Britons, live with a recent past of invading soldiers in their homelands. No invaders have attacked America since 1812. Walter Russell Mead of the Council on Foreign Relations calls the result a "myth of virtuous isolation". It has long been part of what makes America different.

A year ago, that myth was shaken. Stripped of their blanket of distance and inviolability, Americans found themselves at war in Afghanistan, and possibly about to widen the conflict to Iraq. They also began, albeit modestly, to flirt with some of the characteristics of a nation organising itself for war at home: tightening security, sometimes at the cost of civil liberties, and creating a new government department for homeland defence. By introducing Americans to an experience already shared by others, the attacks made America more like the rest of the world. At the same time, they tested—and, in some ways, reinforced—the nation's sense of itself as a place apart.

In his 1996 book "American Exceptionalism", Seymour Martin Lipset argues that Americans "exhibit a greater sense of patriotism, and of belief that their system is superior to all others...than the citizens

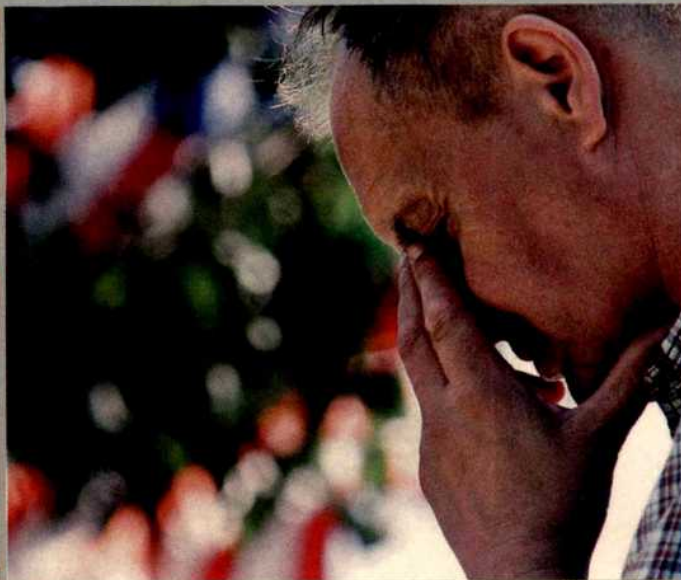
of other industrialised democracies." Opinion polls in the mid-1990s confirmed this. "Do you think your country is better than any other?" Yes, answered 80% of Americans. "Would you rather be a citizen of your country than any other?" Yes, said 90%. "How proud are you of your nationality?" Very proud, said 86%.

Even before September 11th, therefore, Americans were easily the most patriotic nation in the world (in contrast, only 54% of Britons and 35% of the French said they were proud of their countries). After September 11th, love of country went off the scale. "Do you think Americans are more patriotic than before the attacks?" Yes, 85%. "Do you think Americans have appreciated their country more?" Yes, 87%. Since American patriotism is closely associated with optimism—logical enough, if yours is the best country in the world—there was a spike after September in the number of people who thought the country was going in the right direction.

Americans have long been unique among democracies for their religiosity: 36% say they think the Bible is the literal word of God, half say they think America enjoys divine protection. After September 11th, 78% said they thought religion's influence in public life was growing. Books on the apocalypse became bestsellers.

Post-September patriotism was also a coming together. In particular, it meant celebrating the blood-and-guts virtues of blue-collar workers—the firefighters and police officers who don't design computer programs but who ran into the World Trade Centre to save lives. Three hundred and forty-three firemen died in New York on September 11th. Theirs was not a world where bosses make off with billions while the workers lose their pensions. A fifth of them were chiefs, captains and lieutenants who died with the rank and file.

The measures of optimism and church-going have since fallen sharply, suggesting



▶ that part of the post-September rally was the temporary reaction of an outraged nation. Even so, some effects have lasted: this year, for instance, the army met its recruitment target in record time, suggesting that the obligations of citizenship were being taken up more enthusiastically. More important, the intensity of the reaction reminded Americans of some old-fashioned virtues: love of country, respect for religion, social cohesion.

The patriotic affirmation did not therefore produce anything very new. It merely strengthened old mentalities and deep-seated beliefs. In that sense, the impact on America's view of itself was modest. The effect on America's view of the world may prove, in time, more profound.

The froth blown away

Changes to domestic politics were less dramatic than many had expected. True, Donald Rumsfeld usurped Gary Condit in the nation's attention. People talked about burqas, not Monica Lewinsky's dress. Public service came to seem more important (and, after Enron, more honest) than commercial life. Rather as the attack on Pearl Harbour had shaken America out of its self-absorption after the booming 1920s and the Depression, so September 11th did the same for the boom and bust of the 1990s. The heady enthusiasm for Pets.com or Napster seemed faintly embarrassing.

Much of this was merely a matter of blowing away the froth from the 1990s. Not all of it was connected with September 11th, anyway. And in some respects the "new seriousness" has proved temporary. Americans' interest in foreign news, for example—intense in October and November 2001—faded quickly.

The same was true of party politics. Because September 11th reaffirmed old attitudes rather than created new ones, political life changed comparatively little. In the weeks after the attacks, there was some

hope that partisanship would be limited; that trust in government would be restored; that national security would establish itself at the heart of political debate; and even that the so-called "50:50 nation"—the electoral divide revealed by the 2000 election—would be mended. None of this happened.

Mid-term elections are two months away, and the main issues in the public mind are the economy, corporate corruption and health care. The two parties are again deadlocked. After the attacks, public confidence in the institutions of government briefly surged: trust in the presidency, Congress and public service itself all soared to levels last seen in the 1960s. Yet, with the partial exception of the president's own popularity, those measures have returned to normal.

America is barely recovering from recession, but this has little to do with September 11th. The downturn had started well before that day, and the recovery began soon afterwards. The weakening of the economy that took place this year has had more to do with Ken Lay, Arthur Andersen and WorldCom than with Osama bin Laden or al-Qaeda. The direct economic impact of September 11th was minimal, though the indirect effect—particularly the splurge in government spending that resulted—may affect the economy for some time.

So it was not exactly as if the attacks of September 11th had never happened. Rather, it was as if they had been a bolt of lightning that brilliantly and briefly illuminated the landscape without changing it. The storm passed. President Bush called upon Americans to go back to shopping and air travel, not to make special sacrifice for war. In some ways, there seems little that is new in post-September America. But if that was so domestically, internationally things were very different.

To the Bush administration, the attacks

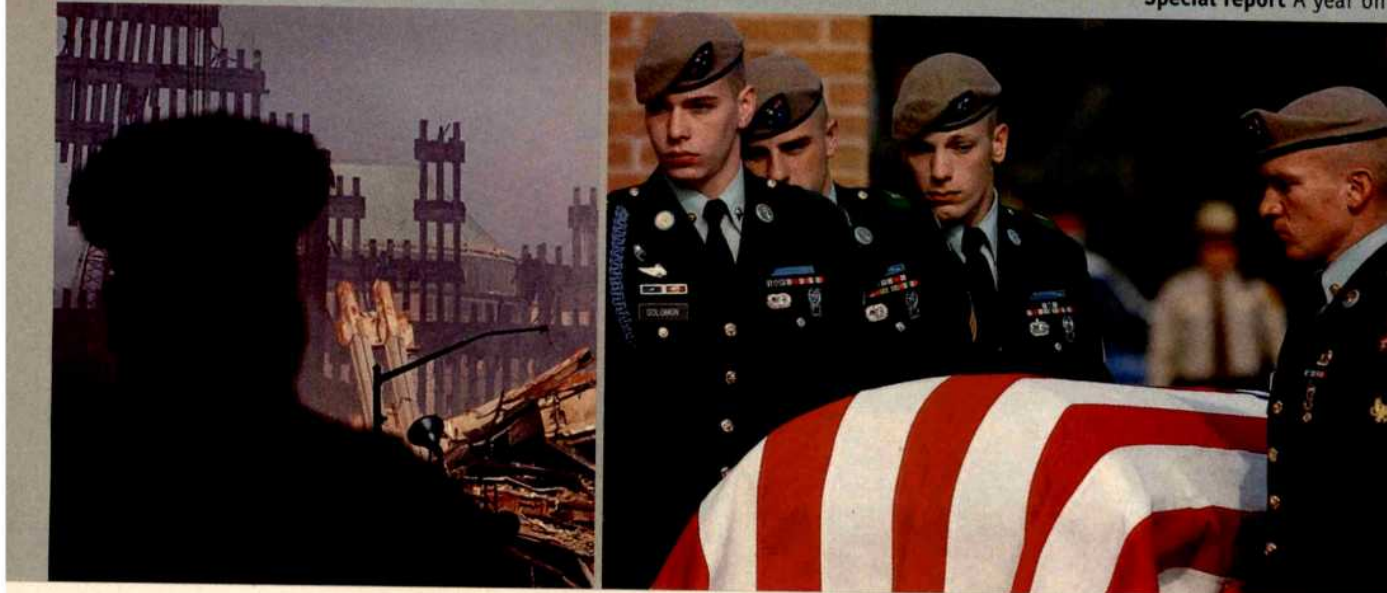
ushered in a new era in international relations. "I really think this period is analogous to 1945-1947," said Condoleezza Rice, the national security adviser, "in that the events started shifting the tectonic plates in international politics." She was exaggerating a bit. Some shifting had begun long before. But, by and large, she was right. America found itself wanting to reorder the world—a world that, in some respects, proved surprisingly receptive to that aim.

Once in a lifetime

Nobody was quicker to respond, or more decisive in pushing through policy change, than Russia's president, Vladimir Putin. He accepted the abrogation of the 1972 anti-ballistic missile treaty, the deployment of American soldiers in the former Soviet republics of Central Asia and Georgia and the possibility of a big expansion of NATO.

Conversely, few countries were more nervous about the new conditions, or more hesitant about policy changes, than members of the European Union. When Mr Bush called the war against terror "the focus of my administration", he made explicit what had been evident since the end of the cold war: Europe is no longer the front line of the strategic struggle that fires the American administration. That did not mean it was irrelevant; since September 11th, intelligence-sharing has deepened dramatically. But it meant that the transatlantic partnership was no longer at the centre of America's world view.

Surveying this fluid scene, Ms Rice argued that it offered a once-in-a-lifetime opportunity. "It's important to try to seize on that and position American interests and institutions before they harden again." In grabbing this chance, the administration, rather like the public, reverted to type—to a take-it-or-leave-it unilateralism tempered by occasional confusion within its ranks. In this respect, at least, there was



► a kind of continuity even in foreign policy.

Soon after September 11th, John Gray, a British historian, claimed that "the era of globalisation is over." Two months later, members of the World Trade Organisation, meeting in Doha, launched a new round of trade liberalisation. They did so partly in response to September 11th. Bob Zoellick, the United States trade representative, argued that freer trade was part of the fight against terrorism. Despite financial meltdowns in Latin America and the administration's politically-motivated espousal of steel- and farm-protectionism, September 11th did not slow the pace of globalisation.

More broadly, there have been no signs of the administration retreating into 1930s-style isolationism. In the months after September 11th, Mr Bush proposed increasing development assistance by 50%. He sent troops to countries as far apart as Colombia, Pakistan and the Philippines. As Jessica Mathews, the president of the Carnegie Endowment for International Peace, argues, "the most dramatic effect of this year has been the tremendous extension in America's foreign engagement."

But this did not mean the administration was toning down its earlier unilateralist impulses. Rather, that patriotic upsurge reinforced its America-firstism, shaping its responses and explaining why it acted as it did. This is why the reassertion of American exceptionalism had big foreign-policy consequences.

Take the outbreak of patriotism first. This was a reminder that Americans, more than Europeans, see the nation as the ultimate repository of sovereignty and law. They may argue about the extent of federal powers. But Americans remain out of sympathy with European notions of international law or pooled sovereignty. Indeed, their constitution forbids the transfer of Congress's sovereign powers. America's own system is best.

Against a background of renewed patriotism, it was hardly surprising that an administration which was anyway inclined towards unilateralism made few moves towards multilateral engagement. It fought bitterly against the establishment of the International Criminal Court, rejected suggested new enforcement provisions for the Biological Weapons Convention, and refused to send the comprehensive test-ban treaty to the Senate a second time for ratification. And it raised the theoretical possibility of designing and testing a new generation of nuclear bombs.

This has dashed broader hopes that America might create a global alliance against terror, which the president himself had raised when he told cadets at the Citadel, a military school in South Carolina, that "a new threat to civilisation is erasing old lines of rivalry and resentment between nations." In fact, the administration made little attempt to put that into practice. By raising the stakes, September 11th may have made the administration more, not less, determined to pursue its national interests in its own way.

Evil and its variants

The second aspect of American exceptionalism—its religiosity—explains some of the confusions of recent policy. American foreign policy has long had a strong moral component. Enemies are not merely threats to national security. They are evil. Mr Bush created an axis out of it, a phrase that made more sense to Americans than to anyone else. There is no such thing as a friend of convenience. "You are either with us or against us," said Mr Bush.

The inevitable result was confusion in dealing with countries that did not fit into either category, such as Saudi Arabia. There was confusion within the administration because, at least at the State Department, the demands of realpolitik and diplomacy conflicted with the impulses of

morality. And there was an even greater degree of uncertainty in handling Israel and Palestine because, in addition to the intrinsic difficulties of that conflict, the administration was now influenced by the louder voices of those urging it to go from being an honest broker in the region to a unquestioning supporter of Israel.

Lastly, the attacks of September 11th brought to the surface a quality that has been forgotten recently about America. Unlike any other democracy, with the possible exception of Britain, America has a strong war lobby. Americans tend to believe wars settle things. They are willing to support vast military spending and to see the most fearsome weapons deployed.

This is the opposite of what was universally believed. After the humiliating retreat from Somalia, and the initial refusal to put troops into the Balkans, America came to be regarded in some quarters as a paper tiger—fierce-looking but unwilling to fight. Mr bin Laden taunted Americans as cowards. In fact, as Mr Russell Mead points out, where the deepest issues of national security are involved, the American public has been willing to take, and inflict, enormous casualties. It had few qualms about bombing Japan; it sustained heavy casualties in Korea; and public opinion supported even the Vietnam war almost to the end (though elite opinion certainly did not). Now, almost 60% of Americans say their country should attack Iraq even if that means heavy casualties.

After Pearl Harbour, Admiral Yamamoto, the architect of that raid, admitted he had "awakened a sleeping giant and filled him with a terrible resolve." A year after September 11th, Mr bin Laden may have done the same. The consequence has been lethal for the Taliban and parts of al-Qaeda. It is not comfortable even for allies. But, given what America is, it was probably inevitable. And for the defeat of global terrorism, it may also be necessary. ■



Central Asia

Back into the cauldron



September 11th has brought America back to a fragile region after a damaging decade of absence. Long may it stay there

IN FEBRUARY 1989 the last Russian units withdrew from Afghanistan across the Friendship Bridge into Uzbekistan, then still part of the doomed Soviet Union. To America, this was a moment of triumph. For ten years, by arming and assisting the *mujahideen*, it had first contained and then reversed what many feared was a Russian drive to the Persian Gulf.

Almost immediately, though, America's interest in the region evaporated. Little American, and not much international, effort was expended on stabilising liberated Afghanistan, which immediately lapsed into civil war. Pakistan, which was once a vital ally in the battle for Afghanistan, was disregarded. Only a year later, the administration of George Bush senior declined to certify Pakistan as free of nuclear weapons, thereby freezing weapons sales to the country. Pakistan's nuclear programme had not seemed such a problem in the 1980s.

The decade of American disengagement proved devastating to Central Asia. The Afghans, exhausted by warlordism, welcomed the rule of the Taliban. In turn, the Taliban's leaders fell under the sway of Osama bin Laden and his al-Qaeda fighters. Long before the attack on the World Trade Centre, these allied groups attempted to spread *jihad* throughout the region, assisting radicals in the former Soviet Central Asian republics, in Kashmir and even in China. Pakistan suffered particularly badly. Cast adrift by the West, which now found India more attractive, it too

moved ever closer to fundamentalism.

September 11th has re-established the precept that Central Asia is too important and too dangerous to be ignored. It is home to the world's most alarming Islamic sects, it is the place where the West has historically rubbed up against Russia and China, and it is both blessed with oil and cursed with (Pakistani) nuclear weapons. By bringing America back to the region in force, renewing the American alliance with Pakistan, conducting "regime change" in Afghanistan and, for the first time, securing American footholds in Uzbekistan and Kirgizstan, last September's terrorist attacks may have the eventual effect of bringing stability to a highly volatile part of the world. That will only happen, though, if America's interest in Central Asia does not dwindle again.

Cautious imperium

So far, the signs are mixed. President Bush has vowed not to abandon the people of Afghanistan, and General Tommy Franks has talked of staying there a long time. Although the defence secretary, Donald Rumsfeld, is not keen on nation-building, he recently announced that his troops were shifting from cave-clearing to more civilian duties. Last week came murmurs that the Pentagon might be prepared to see an extension of the UN's peace-keeping mission in Afghanistan beyond the capital, Kabul. But it is not a priority.

Generous amounts of money—\$4.5 billion or so over the next five years—have

been pledged by America and its allies. Little has yet been delivered, though the Americans have disbursed \$350m and are putting pressure on others to do so. Efforts to integrate into a national professional army the dozens of private armies behind the warlords are underfunded and limited in scale. Only a few hundred men, of the 80,000 or so needed, have been trained so far. To critics like Richard Holbrooke, a former American ambassador to the UN, it is all a world away from the huge international effort made at the end of the Yugoslav wars to stabilise Bosnia—with much success. If it is half-hearted in the exercise of its imperium, America may blunder into a quagmire.

Yet the critics underestimate how much has been achieved. Diplomatic deal-making by an engaged America proved crucial, time and again, to ensuring the birth and survival of at least a semi-functioning government in Afghanistan, led by a Pushtun, Hamid Karzai. This government is still far too dominated by the Tajik minority who made up most of the Northern Alliance, America's chosen allies in the war against the Taliban. But Mr Karzai is gradually appointing more non-Tajiks: and besides, the government is only provisional, until elections can be held in 2004. At that point, the Pushtuns' greater numbers will tell. The former king, furthermore, has been brought back to his capital, though not to his throne or even to a ceremonial presidency, as would have been better. The new government has at least the promise of large sums of money, and the UN, on the back of that, is piling in people and resources. Most telling of all, more than a million Afghans have returned home after a decade in squalid refugee camps.

Though the country is still far from safe, it has not yet reverted to the violent warlordism of the 1990s. That is why refugees dare to return, and why aid workers are able to work—though there are troubles in ▶▶



► some areas, especially the north, where a few NGOs have ceased their operations. Coalition troops, ostensibly there only to hunt for Taliban and al-Qaeda, have helped to calm things. Of course, the effect would be greater if they were dispersed all around the country, rather than concentrated along the Pakistani border. America would do better, too, to stop collaborating with warlords in pursuit of the war on terror. Still, one might almost call this nation-building by the back door.

Like it or not, America has now become an activist power in Central Asia—though it ought to go much further. The fact that neither Russia nor China has raised serious objections to America's appearance suggests that they, too, see merit in having the superpower involved, though they would not care to see it stay. Even Iran—or at least the moderate half of its government—has quietly acquiesced.

Despite the embarrassing fact that neither Mr bin Laden nor the Taliban leader, Mullah Omar, has been captured, the main purpose of the American action has been achieved: both men have been driven out of their strongholds, and, even if alive, are far less able to spread terror. This is good news not just for Afghans and Americans, but for Pakistan and the rest of Central Asia.

Our sonofabitch

But if America has, at long last, reversed its neglect of the region, it is also in danger of committing another old mistake—embracing too closely unsavoury types with a precarious grip on power. America's presence brings benefits, but it also rouses hatred, especially when Washington appears to be propping up despots. Pakistan provides the most worrying example.

Ever since the start of the American action against Afghanistan, when General Pervez Musharraf decided to allow his territory to be used to mount raids against the

Taliban, the terrible fear has been that a backlash of Islamic rage would sweep the general's government away. The thought of Pakistan's nuclear weapons and its long-range missiles in the hands of extremists is chilling. Is it plausible?

Certainly, the risk exists. Many hundreds of al-Qaeda and Taliban are known to have escaped from Afghanistan into Pakistan, where they are hiding in tribal areas that are not fully under the control of the government. They have linked up with Pakistani groups active in Kashmir, and there is some evidence that they may be trying, through attacks in Kashmir, to provoke a war with India in the hope of seizing power when, as they suppose, Pakistan is defeated. In the meantime, they are driving overseas businessmen and investment out of the country with attacks on Christian churches and foreigners.

General Musharraf seems unable, or unwilling, to crush these groups. No sooner does he ban one, such as the most notorious, Jaish-e-Muhammad, than most of its people pop up again under another name. He has failed to end cross-border attacks on India—though the Indians suspect that this is less because he cannot than because he does not want to. The groups have their uses, such as bleeding India in Kashmir, as well as their dangers.

For the general, the rewards of his embrace of America have been lavish: billions of dollars in new loans, a rescheduling of IMF debt, a lifting of sanctions and much else. The former pariah now finds himself a hero in Washington. None of this, however, can protect him from his Islamic enemies. In numbers, they are few; but the risk of an assassination, or a coup led by pro-Islamic officers, remains. The general is becoming more dictatorial: the long-awaited elections due next month promise to be a farce, with opposition leaders barred and the parliament already emasculated.

Most mainstream Pakistani opinion supports the alliance with America, and the general has been foolish to fall foul of it by his anti-democratic manoeuvres. They have united everyone against him: the Islamists, moderate and radical, as well as the secular parties, especially those led by the former arch-rivals, now allies, Benazir Bhutto and Nawaz Sharif. The further General Musharraf drifts from democracy, the more untenable his position will become.

The questionable Stans

In the former Soviet Asian republics, America has had to acquire some even nastier new friends. Islam Karimov, the president of Uzbekistan, and Askar Akaev, the president of Kirgizstan, have both provided air bases. In both countries, the past year has seen a further deterioration in already grim human-rights records, despite criticisms by the State Department.

The growing despotism of Mr Karimov and Mr Akaev is clearly bringing problems in its wake. In both countries, the economy has weakened, and support has increased not only for secular opposition groups but for more alarming religious movements such as Hizb-ut-Tahrir, which has been attacking the American presence in Kirgizstan. Uzbekistan, in particular, has jailed many thousands of moderate Islamists, an excellent way of converting their families and friends to extremism. In Kirgizstan, one leading opposition figure has been detained, another has died on hunger strike, and the government has yet to set up a fair inquiry into the killing by police of at least six unarmed demonstrators in March.

On the other hand, the American campaign in Afghanistan has badly hit the most dangerous of those religious groups, the Islamic Movement of Uzbekistan (IMU), which aims to establish an Islamic caliphate throughout the region, and used to stage raids from its secure bases in Afghanistan. The IMU's military leader, known by the *nom de guerre* of Juma Namangani, has almost certainly been killed. In the immediate future, there would appear to be no significant threat to any of the Central Asian regimes, though it is hard to see how they can be reliable allies in the longer term.

The American presence in the "Stans" is hugely beneficial to countries that are suspicious of Russia and China. That gives America bargaining power. And when all is said, Central Asia is in far better shape than it was a year ago. But Afghanistan could revert to its murderous past form at any time, Pakistan gives genuine cause for concern, and the leaders of the former Soviet republics need to be pressed towards better behaviour. If America fails to follow through on what it has begun, the consequences will be dire. If it stays engaged, and shoulders its burden, the next decade could be a lot better than the last. ■



The Arab world

Revolution delayed



An American strike on Iraq will not ignite the Arab street. On the contrary, it may nudge some societies towards the modern world

IT TOOK less than a year for the felling of the twin towers to transform the political geography of Central Asia. But it was not, of course, the people or the grievances of Central Asia that lay behind the attacks on America. All the suicide attackers were Arabs. Fifteen of the 19 were Saudi Arabians, like Osama bin Laden himself. In the year ahead, the biggest consequences of the attacks on America are likely to be felt in the Arab world.

Mr bin Laden (if he is still alive) might welcome that. Possibly, he intended all along to draw America into an Islamic civil war. His aim, in the view of Michael Scott Doran, professor of near-eastern studies at Princeton University, was to provoke an international military crackdown, which he and his followers could exploit for their particular brand of revolution.

"The script", says Mr Scott Doran, "was obvious: America, cast as the villain, was supposed to use its military might like a cartoon character trying to kill a fly with a shotgun." Muslims everywhere would be shocked by how nonchalantly America caused their brothers in the faith to suffer and die. That would open a chasm between state and society in the Middle East. Governments allied with the West, many of them repressive and corrupt, would drown in a sea of hostile opinion.

Are events following Mr bin Laden's script? Not quite. Or, safer to say, not yet. America's war against the Taliban in Afghanistan did indeed anger many Muslims. It rocked the House of Saud. It made

General Pervez Musharraf feel he had to tighten his military dictatorship in Pakistan. But no regime friendly to the West has yet been swept aside by a tide of Islamic rage. So far as any outsider can discern, none looks even near that point.

What this suggests is that if the American cartoon character packed up his shotgun and walked away now, the Arab world might well plod on in its familiar pattern, pretty much unscathed by September 11th and all that flowed from it. But George Bush's administration shows little desire to turn its back, or its cheek. It is, rather, marching towards Iraq and the sound of gunfire. The big question now is therefore whether an American-led war to remove Saddam Hussein will give Mr bin Laden the victory he was denied when the Americans removed the Taliban.

The word on the street

In truth, nobody knows. The famous "Arab street" is undoubtedly hostile to the notion of America waging war in Iraq while appearing to do so little to impose peace in Palestine. But since when has public opinion changed regimes in the Arab world? Iran had a popular revolution against the shah in 1978. But one of the most striking things about the recent history of the Arabs is the durability of the supposedly fragile monarchies and dictatorships that misgovern them.

Jordan, arguably one of Iraq's most vulnerable neighbours, is a prime example. More than half its people are Palestinians,

who in the 1970s fought a civil war with the other half. The little country has seen riots and assassinations. For all that, the Hashemite family which the British installed as monarchs of the country Winston Churchill invented in the 1920s has stayed in power ever since. King Hussein lost a war, east Jerusalem and the West Bank, to Israel in 1967, but remained on the throne. He also remained when he made an unpopular peace with the Israelis in 1994. After his death in 1999 the succession passed smoothly to his equally pro-western son, Abdullah.

Jordan is by no means exceptional. The scions of Ibn Saud have controlled the Arabian peninsula and its oil wealth for a century. And in recent decades the formerly "revolutionary" republican regimes of Egypt, Syria and Iraq itself have settled down to an outwardly stable dynastic rhythm. Hafez Assad ruled Syria for 29 years and then bequeathed absolute power, as if the country were a private possession, to his son Bashar. The assassination of Anwar Sadat by Islamic militants in 1981 did not prevent his deputy, Hosni Mubarak, from assuming the presidency of Egypt and clinging to it ever since. A junior Mubarak is now being groomed to take over. Mr Hussein himself has been Iraq's absolute ruler for almost a quarter of a century, and a favoured son, Qusay, stands ready to inherit. The popularity of these regimes may wax and wane—but, practised in repression, they have never relied on popularity in order to survive.

This is not to say that they can survive unchanged forever. Nor should they: having crushed freedoms, squeezed the breath out of opposition parties, and in most cases delivered precious little prosperity by way of compensation, it would be disappointing as well as peculiar if they did. But why expect an American war on Mr Hussein to start knocking over dominoes that managed somehow to stay upright ►►



▶ despite Arab-Israeli wars, the Iranian revolution, the Iran-Iraq war, the Gulf war and two Palestinian *intifadas*?

Millions of Arabs, it is true, admire the Iraqi dictator's defiance of America and Israel. That does not mean that they would respond to his downfall by marching on their own governments. Many of those who admire him from afar are at the same time shrewdly aware of how dreadful it is to be an Iraqi. This is why Mr Hussein has never attained the status of a Nasser, who until the 1967 defeat by Israel was a genuine hero to all Arabs. Nor, having for most of his career espoused the secular nationalism of Baathism, can Iraq's dictator convincingly pose, like Mr bin Laden, as a champion of the Islamic alternative. It is anyway far from obvious why the average Egyptian or Saudi would blame his own government for an American attack on Iraq. These supposedly pro-American governments have already taken evasive action by making their own opposition to such a war crystal clear.

Given all this, the prospect of Arab regimes collapsing the moment America strikes Iraq looks fairly remote. It would be even more remote if America won swiftly, without inflicting heavy casualties. Since a war in Iraq entails so many imponderables, it would be folly to be confident of such a victory. But it would also be foolish to rule the possibility out. In Afghanistan, American technology soon dismantled the enemy's will to fight. And there is plenty of evidence from the Gulf war that the will of many Iraqis to fight for Mr Hussein has limits. Most of his soldiers surrendered at the first opportunity. Many of his civilians then tried to overthrow him. Abandoned by America, at the behest of Saudi Arabia, their uprising was crushed. The subsequent repression has not diminished their loathing of the man.

That Saudi request, in 1991, for the Americans to leave Mr Hussein in power,

is telling. Are Arab rulers afraid that a war will go horribly wrong—drawing in Israel, bringing pro-Saddam protesters on to their own streets, provoking a post-war civil war inside Iraq, accelerating its collapse into warring sectarian fiefs? Or are they afraid of the opposite: that the war will go horribly right?

The latter, say members of the Iraqi opposition in exile. They, of course, have an interest in saying so. All the same, the Iraqi National Congress, the umbrella group that represents most of the opposition factions, has drawn up what looks like a promising blueprint for a post-war Iraqi order. It is based on two ideas: democracy and federalism. The opposition argues that as a nation with deep national and sectarian divisions—Shias, Sunnis, Kurds—Iraq can stay whole only by loosening the grip of the centre and devolving power to autonomous provinces.

Awkward for some

This idea has special resonance with Saudi Arabia. It is, in point of fact, anathema. Like Iraq, Saudi Arabia is a complex tribal society, which has resolved its problem of diversity by imposing authoritarian control. The Saud family enforces its will from the centre, deriving legitimacy from its claim to implement *sharia* law and represent the global interests of Islam and the *ummah*, the community of believers. Against such a background, Saudi Arabia's misgivings about an American war in Iraq are understandable.

An unhappy ending—one, that is, in which Mr Scott Doran's cartoon-character America follows the bin Laden script and nonchalantly causes Muslims to suffer and die—would strengthen the feelings of those Saudis already sympathetic to al-Qaeda. If Iraq disintegrated, the Shia population of Saudi Arabia might follow the Iraqi example and start to think about secession too. As for what the West would

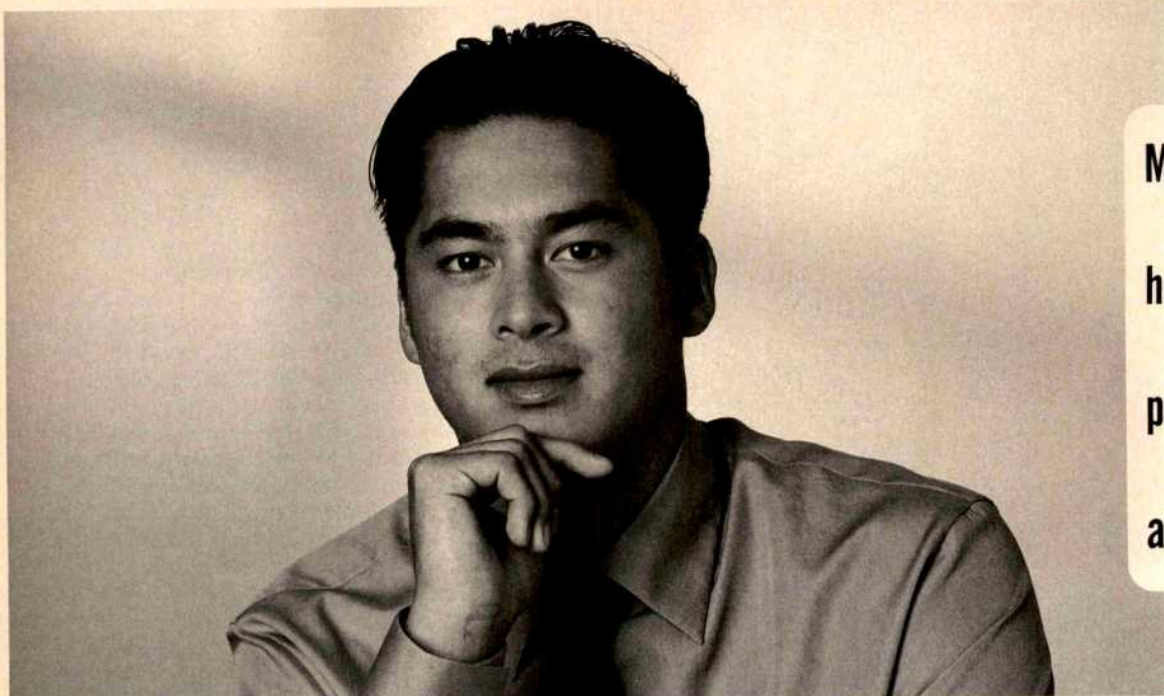
construe as a happy ending—the emergence of a federal democracy in Iraq—this would complicate the Saud family's efforts to maintain its totalitarianism. In its heart, the House of Saud wants nothing to change and history to stop.

The Saudis are not alone in that. Many of the critics of an Iraqi war in the West also say that it will bring instability, implying that the stability of the Arab world is a self-evident good. The paradox is that most ordinary Arabs privately concede that the form of stability provided by the Assads, Husseins, Mubaraks and Sauds is not so good, a blend of corruption and repression that has succeeded mainly in holding the Arabs back. Might the chasm which Mr bin Laden planned to open between state and society in the Islamic world turn out to be highly desirable, if—contrary to his script—it encouraged a turning towards political modernity?

It is possible. The suicide bombers of al-Qaeda made the opposite judgment, reckoning that by drawing America into action against Muslim countries they could win recruits for an Islamic revolution. America has certainly not made itself popular in the Muslim world since September 11th, and may become less popular still in the course of a military intervention in Iraq. On the other hand, the Arab perception of America's aims could swiftly change if (as is probable) the Iraqis were then to celebrate the downfall of Mr Hussein as joyfully as Afghans celebrated the downfall of the Taliban; and if (as is possible) America followed up quickly with an intensified push towards peace in Palestine.

Many westerners would call this wishful thinking. In fact, it is less fanciful than the idea that Islamic radicalism is poised to overthrow the secular regimes of the Arab world the moment America gives Iraq a push. Violent Islamic radicalism of the al-Qaeda sort has been in decline in most parts of the Middle East for at least two decades, and no amount of anti-American feeling seems likely to switch this trend abruptly into reverse. Armed Islamic movements have been suppressed in Egypt and Algeria. With the possible example of Hizbullah in Lebanon, Arabs never imported the Islamic revolution preached from Iran, and Iran itself is now retreating from it.

"Violence", argues Gilles Kepel, a professor at the Institute for Political Studies in Paris, "has proven to be a death trap for Islamists as a whole, precluding any capacity to hold and mobilise the range of constituencies they need to seize political power." Arabs are no fools. The violence and audacity of September 11th may have captured the imagination of many of them. Far fewer believe that waging war on America and turning their back on modernity is a cure for their desperate problems at home. ■



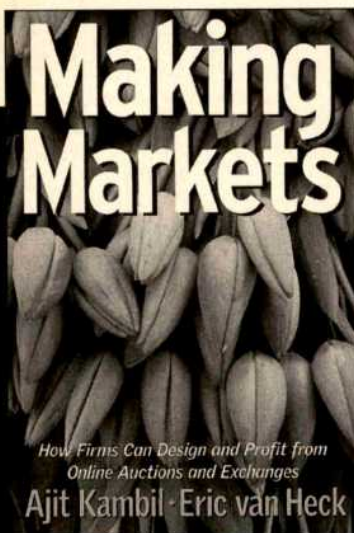
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BATTICALOA AND COLOMBO

But what will life be like if the Tamils win their homeland?

IT COULD be "the best news to come out of South Asia in a long time." So says a diplomat of the peace talks between Sri Lanka's government and the Liberation Tigers of Tamil Eelam (LTTE) that are scheduled to begin in Thailand on September 16th. On September 4th the Sri Lankan government un-banned the LTTE, one of the world's bloodiest insurgent groups. There are qualms about handing over territory to the group that perfected the craft of suicide bombing, murdered two heads of government and has liquidated any Tamil of significance who is more moderate than its reclusive leader, Velupillai Prabhakaran. But for now the Sri Lankan government, foreign powers and most Sri Lankans themselves seem willing to suppress those qualms. The prize is an end to 19 years of war between the government, which represents mainly the island's Sinhalese majority, and the Tigers, defenders of the aggrieved Tamil minority.

The war, which has killed some 65,000 people, has been bloodier than its causes seemed to warrant. Its origins lie in misguided attempts by earlier governments to promote Sinhalese interests at the expense of Tamil ones, especially by discriminating against the Tamil language. The Sinhalese have long been willing to make

amends, largely by devolving power to the north-east, which the LTTE deems the Tamils' Eelam (homeland).

The characteristics that make this conflict one of the few with a prospect of resolution also make the solution potentially troubling. Last December Sri Lankans elected a government willing to hand over the north-east to an interim administration controlled by the LTTE. Big issues, such as how the north-east will fit into Sri Lanka's constitution, are to be worked out later. This arrangement may well buy peace. What it may not buy is freedom and security for the 2m or so people who would then be living under LTTE rule. Even for Tamils, life under the Tigers might be grimmer than it was under the Sinhalese-dominated government, vicious though its record has been. The government's trickiest task is to secure the rights of north-easterners without provoking the LTTE into resuming the war.

There is no mistaking the relief that peace has brought. People in the north-east celebrate the ten-month-old truce, which has silenced gunfire, lifted curfews and freed travel between "cleared areas" (controlled by the government) and "uncleared" ones, the domain of the LTTE. "The fear is gone," says Arulanantham, a

Tamil jeweller in Batticaloa, a big eastern town controlled by the government. Throughout Sri Lanka, more than 100,000 displaced people have returned to their homes or are on their way. In Jaffna, the Tamils' cultural capital, the price of mangoes has quintupled with the reopening of access to the southern market. Farmers in the region are once again threshing their paddy crops at night.

Yet in the east, tension between peace and rights is already acute. Unlike the north, which is now almost purely Tamil, the east still has large Muslim and Sinhalese minorities. Here, relief is tinged with anxiety. Muslims in Kattankudy, near Batticaloa, have not forgotten that the LTTE slaughtered a mosque-full of people in 1990. They want to be governed by an authority separate from the interim administration, a concession the Tigers are highly unlikely to grant.

Tamils in uncleared areas already know the LTTE's ways. A woman hitchhiking with two companions turns out to be on her way to appeal to the LTTE to release her 17-year-old husband, who was locked up for desertion. A quarry worker near Batticaloa sent his son abroad after he escaped the LTTE's clutches; the father has since been detained six times. "People are scared," he says.

Under the agreement with the government that Norway brokered, the LTTE is now free to operate politically in cleared areas. In Batticaloa it does more than that. It has drafted some children and imposed an extra 8% "tax" on civil servants' salaries. Last month the Tigers raided a Tamil newspaper, tying up its journalists and stealing equipment. Once the government pulls »



out, handing over power to an LTTE-controlled administration, worries B. H. Miller, an outspoken Jesuit priest in Batticaloa, it will be "the death of democracy."

So can the government preserve both peace and democracy? Or will it, in effect, settle for one country with two systems, a militarised autocracy clamped on to the relatively democratic south? The foreign minister, Tyrone Fernando, insists that the "whole purpose" of the peace process is to "get [the LTTE] to come into the democratic process and to give up reliance on arms." But its critics say the government, led by the business-backed United National Party, is over-eager for a deal. The prime minister, Ranil Wickremesinghe, has said that he will talk to the Tigers about anything but secession. The interim administration, when it comes, will not be an elected body. The closer talks get to such issues as democracy and disarmament, the stickier they will become. The government needs them not to get stuck. Last year, the economy shrank for the first time since independence.

The soft-peddalling of principle makes some Sinhalese nervous and the opposition aggressive. Many sceptics believe that the truest signs of the LTTE's intentions are its continued recruitment of children and the aggressive propaganda videos it screens, even in cleared areas, of its military exploits, including last year's attack on the airport in Colombo.

Scepticism could become obstruction, or even revolt. The president, Chandrika Kumaratunga, who leads the main opposition party, has the power to derail the peace process, for example by dissolving parliament early. Mr Wickremesinghe wants to curtail this power by constitutional amendment. This week a compromise looked likely, but the president will remain a potential troublemaker. A scarier strain of opposition could come from the JVP, a once-violent party that espouses an odd mix of Marxism and Sinhalese nationalism. Thousands of its supporters demonstrated in Colombo on September 3rd against concessions to the LTTE.

But the settlement may be less a surrender than many people fear. The LTTE, though ruthless and well armed, is also impecunious, an embarrassment the government intends to exploit. Contributions from the Tamil diaspora are down—but fighters' pay and widows' pensions are not. Financial leverage will be "an important factor," says an official. Aid to the north-east will come through the central government with strings attached and donors to monitor how the money is spent.

The LTTE must also contend with outside powers, particularly the United States and Britain, which do not intend to un-ban the Tigers just yet and would probably arm the government if they resumed fighting. The Sri Lankan Monitoring Mission, a Norwegian-led group that observes both sides' adherence to the ceasefire, human-rights NGOs and the swelling flow of people between the north-east and the south will all help tame the Tigers. Under their gaze, recruitment of child soldiers has lately dipped in the east. Ordinary Tamils, most of whom are grateful to the LTTE for fighting the government to the negotiating table, will eventually assert themselves. "If they don't come in the democratic stream, they will not be tolerated by Tamils," says a Catholic priest from Jaffna.

This may produce what a diplomat calls the "sloppy solution"—the gradual democratisation of the north-east through demography, commerce, pressure from abroad and from Tamils themselves. Though worse than a formal settlement, which would lay down democratic rules in the north-east, it would be far better than either war or repression. The question is whether the man with the cyanide capsule around his neck and suicide bombers at his command will let it happen. ■



Prabhakaran, concealing his capsule

Indonesia's armed forces

Khaki power

JAKARTA

Though kicked out of parliament, the army is still a force to be reckoned with

WHEN Indonesia's parliament voted recently to abolish the 38 seats it reserves for the armed forces, pundits hailed the move as proof that the chief instrument of repression during the 32-year dictatorship of Suharto had finally been brought under civilian control. But Indonesian human-rights organisations still insist that the army enjoys unhealthy influence over the government, exploits this to pursue shady businesses, and commits abuses with impunity. This contradiction matters to more than local observers. The United States, too, would like to improve ties with Indonesia's top brass for the sake of the war on terror. But many in Congress are hesitant to resume military aid until it is clear that Indonesia's armed forces have really become servants of the popular will.

Everyone agrees that military influence has declined markedly since the army's heyday under Suharto. Two years ago, it formally renounced its "dual function" as guardian of political probity as well as of national security. The police, once under military command, now report directly to the government. Another reform bars serving officers from posts in the cabinet or civil service, which they used to dominate. Former soldiers are gradually being removed from provincial governorships, too, as their five-year terms expire. The loss of the army's seats in parliament, with effect from 2004, will mark its final exclusion from any overt political role. Agus Widjojo, the head of the military caucus in parliament, says that his fellow officers are happy to go.

But General Widjojo's notion of civil supremacy seems a little unorthodox. He speaks of "mutual respect" between the civilian and military authorities, and argues that politicians should not meddle in operational affairs. The humiliating treatment meted out to the top brass by Abdurrahman Wahid, a former president, justified their open defiance of him, in the general's view. Senior soldiers opine loudly and publicly on security policy. And on the whole, they seem to be getting their way: President Megawati Sukarnoputri's stance on Indonesia's many internal conflicts is far more hawkish than Mr Wahid's was.

Efforts to hold the army accountable for its brutal and often counter-productive handling of those conflicts also seem to have ground to a halt. The special tribunal set up to try those responsible for the devastation of East Timor, a secessionist prov-

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All Mega's men

ince that has since become independent, has so far let off all military suspects scot-free. The attorney-general's office says it has no plans to mount more trials. In other restive provinces, such as Aceh and West Papua, soldiers still run amok, but only a handful of cases has ever come to trial.

The government also seems loth to pry too deeply into military finances. Only about a third of the armed forces' expenditure (no one is sure, since the figures are so opaque) comes from the state budget; they raise the rest themselves, by means both fair and foul. Military foundations run logging concessions, palm oil plantations, hotels, banks, an airline and all manner of other businesses. The army's presence in every district and village of the country (the so-called "territorial system") gives it leverage over local politicians and officials. The army exploits this influence to win lucrative contracts, muscle in on land deals, run protection rackets, set up wild-cat mines, and so on.

But all this is not quite as sinister as it sounds. At the national level, at any rate, the armed forces' apparent ascendancy stems more from a meeting of minds between Miss Megawati and the top brass than from manipulation. She, like her senior officers, is an ardent nationalist, with a hatred of disorder. Furthermore, even on matters of security, the army does not always get its way: take, for example, the government's recent decision to defer a military escalation in Aceh, a step the high command had demanded for months.

What's more, corruption and impunity extend far beyond the army in Indonesia. The government seems just as lenient towards the businessmen who embezzled billions from the central bank, to name just one notorious case. This week, Akbar

Tandjung, the leader of the formerly ruling Golkar party, was found guilty in a large fraud case, but sentenced to only three years in prison—too little, critics said. Some soldiers blame the government for all the armed forces' failings, since it is not pushing harder for reform. That is doubtless a cop-out. But these days, weak civilian leaders do seem a bigger threat to Indonesia than an overbearing army. ■

Japan

Roads to ruin

TOKYO

Koizumi needs to take a new direction

WHICH map is Junichiro Koizumi using? Having wandered a long way from his initial reform pledges, he is now trying to redirect himself by straying overseas, with a trip to North Korea planned for September 17th. The visit, the first by a Japanese prime minister, has given his ratings a boost. But a more reliable route towards enduring popularity exists at home.

Mr Koizumi needs to tackle the problem of the overbuilt network of roads and bridges that criss-cross Japan, often duplicating existing routes or going where nobody wants to drive. The runaway construction that created this mess is one of Japan's most familiar and expensive headaches, and Mr Koizumi pledged to fix it when he took office last year. Since then, however, numerous compromises have sapped his credibility, and a much-touted panel of advisers, which released its in-

terim report on highways last week, is still ducking the most difficult decisions.

While sending them off to finish their work, Mr Koizumi might also take a close look at the second glaring feature on the map: Nagano, a rural prefecture lying to the west of Tokyo, where a reformist governor won a thumping re-election victory on September 1st.

Yasuo Tanaka gained a fresh term by taking precisely the sort of risks that the prime minister has so far avoided. Like Mr Koizumi, Mr Tanaka first got into office by promising a thorough structural overhaul of government, and by distilling these sweeping pledges into specific and pragmatic reforms—most importantly, in Mr Tanaka's case, by vowing to stop the building of new dams. Also like Mr Koizumi, the rural governor has faced a hostile political assembly determined to thwart his reforms. Unlike Mr Koizumi, however, Mr Tanaka has stuck to his pledges despite this, halting construction on two dams and braving a vote of no confidence by the assembly. After refusing to compromise and appealing to the public, he has been rewarded with a convincing re-election.

Sadly, Mr Koizumi has consistently refused that sort of steadfast and edifying approach. He has backed away from dealing with banks' bad loans, and allowed his own party to gut his plans for privatising the postal service. And now he is failing to show leadership on road construction, even though he has said he wants to cut public-works spending. This failing seems even sadder now that the special advisory panel he appointed has helped to generate public outrage about the four public road and bridge corporations that Mr Koizumi says he wants to privatise.

One reason for this outrage is the nature of the panel, which holds its hearings in public and includes among its seven members Naoki Inose, an outspoken author who seems to delight in taking potshots at the highway lobby. The hearings have highlighted the huge losses rung up by the government's road corporations. They have detailed the corruption that allows connected private companies to make extortionate profits through roadside concessions. And they have exposed the dishonesty of the public companies' senior management, which lied to the advisory panel when it asked to be allowed to see their financial records.

As a result, 60-70% of Japanese now say that they would like to see the highway corporations overhauled and the building of new roads scaled back. Yet the details will be tricky—the panel has so far offered little in the way of solutions to the problems it has highlighted—and leave plenty of room for fudge. If highway reform is to matter, Mr Koizumi must recheck his map, grab the wheel of his government and steer it in a clear direction. ■

The first Australians

It's our land

But the aborigines remain poor

MEMBERS of the Larrakia people, Darwin's original inhabitants, raised an aboriginal flag in the city in 1971 and declared their traditional right to a small area of suburban land. This week, their claim to hundreds of acres of undeveloped land—much of it mangrove swamps and bush—in and around Darwin, the capital of Australia's Northern Territory, reached the Federal Court. It is the first "native title" claim over land in a state's capital city to come before the courts.

Native title rights have existed in Australia only for a decade. In 1992, in response to a claim by a group of Murray Islanders led by Eddie Mabo, the High Court reached the historic decision that the islanders were entitled to "possession, occupation, use and enjoyment of the lands in the Murray Islands". The Mabo judgment, which was later incorporated into the Na-



The sound of the suburbs

tive Title Act of 1993, overturned the legal concept of *terra nullius*, that the land belonged to no one until the British arrived in 1788. If indigenous Australians could demonstrate a traditional connection to their land, and as long as the land had not been sold to anyone else or affected by acts of

government, native title could be claimed.

In the current case, the traditional connection of the Larrakia to the land seems clear. They remained on their land as Darwin developed; maintained sacred sites in the city area; and continued to hunt and fish locally. The present case will turn on whether the Larrakia have a legal claim to land that in the past was in private hands, but is now again owned by the Crown.

Yet whatever the outcome of it, the lives of the Larrakia are unlikely to be greatly improved. In the decade after the Mabo case, campaigners for a better deal for aborigines had hoped that things would change for the first Australians. But in 2000 a United Nations' team reported that aborigines still came off badly in employment, housing, health and education. Indigenous communities continue to suffer from disproportionately high levels of poverty, domestic violence, alcoholism, drug addiction and high rates of juvenile and adult imprisonment. An aboriginal man is 17 times more likely to die in custody than a white person, aboriginal unemployment is double the national average, and around 30% of aborigines are affected by diabetes.

While native title can offer a say over running national parks and the ability to negotiate mineral rights, in practice these are not very useful, since most of the land in question is deep in the outback, or, as in Darwin, is undeveloped swamp or bush. Fred Chaney, the deputy president of the National Native Title Tribunal, believes that for native title to do more than just protect traditional lifestyles, the government must help integrate indigenous Australians into the modern economy. If the Larrakia are to become more than "land rich, dirt poor", as a former Northern Territory chief minister once put it, they will need more than a successful day in court. ■

The Internet in China

Stop your searching

BEIJING

Censors clamp down on foreign helpers

CHINA'S industrious Internet censors have hit on a new tactic. Until last week, they had focused on blocking access to websites containing material deemed inimical to the Chinese Communist Party. Now they are targeting search-engines that might lead users to such material. Two Californian search-engines—Google and AltaVista—can no longer be accessed through Chinese internet providers.

Google is particularly popular in China because of its ability to search for pages in simplified Chinese characters. AltaVista also has a Chinese-language capability, but Google not only provides links to web pages, but also to copies of those pages stored on Google's computers. Even if a server is blocked, its content can sometimes still be read.

China has its own search engines, but they do not provide access to web pages stored outside the country. The government would be far happier if foreign search engines followed the example of Yahoo!, an American company whose Chinese search facilities offer sanitised results. A search on Yahoo! in simplified Chinese for the banned Falun Gong sect

found only one web site, that of an anti-Falun Gong group, together with more than 180 news items culled from the official Chinese media. This year Yahoo! signed a pledge circulated by China's government-backed Internet Society which commits signatories not to disseminate information that might threaten state security or social stability.

The authorities are becoming particularly worried about possible threats to stability in the run-up to the Communist Party congress in November, an event which this year will involve extensive leadership changes. The party does not want disaffected groups such as Falun Gong stirring up trouble. Determined users in China, though, will always find ways of skirting around controls. There are ways into Google other than by typing in the regular www.google.com—for instance, by using a numerical address.

An American think-tank, RAND, published a report last week on the Internet in China. It said that while China has done a remarkable job of finding counter-strategies to what it sees as the negative effects of the e-revolution, time is on the side of its opponents.



Arab-Americans

A year of living nervously

DEARBORN AND LIVONIA, MICHIGAN

Arab-Americans are more worried than ever about George Bush, and increasingly puzzled about what being an "Arab-American" means

AT THE end of last month, around 50 Arab-American leaders gathered in Dearborn, Michigan, to meet Jennifer Granholm, the Democratic candidate for governor. The meeting was meant to be a show of strength: there was plenty of talk about Arab-Americans being a crucial swing-group in the state. But this confidence was belied both by events (the previous day, a grand jury had indicted four alleged supporters of al-Qaeda in Detroit) and by the complaints about increased scrutiny from the government. One businessman referred to George Bush's attorney-general as "Ayatollah Ashcroft".

With emotions ranging from anguish to fear, anger and ethnic pride, Arab-Americans are still reeling from last year's terrorist attacks. This tumult has been complicated by an identity crisis. To the extent that they have ever thought of themselves as "Arab-Americans", most see themselves as middle-class Christians (most Muslims in America are black or Asian). But immigration is making the group poorer and more Muslim—thus bringing them a little closer to the stereotypes that many of them dislike.

Has there really been a backlash against Arab-Americans? In the days after September 11th, there were racial attacks, but these became less common once George Bush denounced them. In May, the Justice Department said it had investigated

350 hate crimes since September 11th. By most measures, Arab-Americans and Muslims are safer from racial attacks in America than they are in Europe.

Harassment by the government is a different matter. Arab-Americans think that John Ashcroft's Patriot Act, passed last October with overwhelming support from Congress, was aimed at them. So far, virtually all the people in America who have been investigated and detained under the act seem to have been Muslims.

Many think the idea that Mr Bush has "turned against" Arab-Americans is also born out by his foreign policy. They bitterly resent his "one-sided" support for Ariel Sharon's incursions into Palestinian territory. They are also unsympathetic to the idea of invading Iraq, not least because they fear that any setback for America could result in attacks on their own communities. "If the United States invades Iraq, I wouldn't want to be living in Dearborn," says Terry Ahwal, a leading Palestinian Christian in the Detroit area.

Last October, a survey for the Arab-American Institute (AAI) found that 90% of Arab-Americans were reassured by the president's comments and actions. By May this year, that figure had fallen to 54%. The proportion who reported experiencing discrimination in the past because of their backgrounds remained unchanged at one-third. "I haven't seen anything more arro-

gant than Bush and his clan," says Osama Siblani, publisher of the Arab-American News and a former Bush supporter. "I haven't seen anything less compassionate."

Part of this may be political posturing: for instance, the Democrats are arguably more pro-Israel than the president. But the overall picture of a group that feels under pressure is clear. Ibrahim Kira, a psychologist who treats immigrants at the Arab Community Centre for Economic and Social Services (ACCESS) in Dearborn, points to many cases of severe regression among his patients, after the "double trauma" of September 11th and then the backlash.

A recurring theme among Arab-Americans is what Ms Ahwal calls an "eerie feeling" of being under scrutiny—from police officers, co-workers and neighbours. "If I went to New York and took a picture of the Statue of Liberty, would my neighbour misconstrue that?" asks Ms Ahwal. In Dearborn, Abdallah Boumediene, who works with Iraqi refugees at ACCESS, points out that many of them fled to America to escape persecution. "Now they're finding some of the same things here. Most of their anxiety relates to security matters. They just don't know how to deal with it."

This scrutiny is all the less welcome because many think that they are being pigeonholed as members of a group that they had not identified with. The census lists 1.3m Arab-Americans in 2000 (roughly double the figure for 1980). John Zogby, whose firm conducted the AAI poll, says the true number is more than three times higher (see chart overleaf). He reaches this figure by including more new immigrants, and also by adding in more assimilated descendants of immigrants from as far back as the 1890s.

But has a Christian whose grandfather came from Lebanon really got that much in

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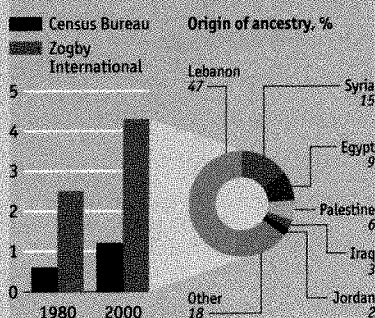
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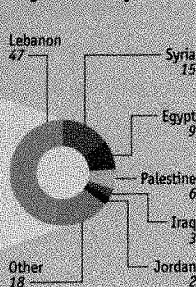
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Divided and worried

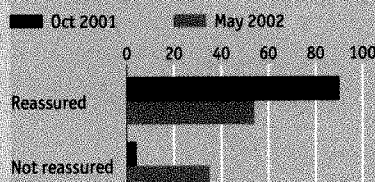
Estimates of Arab-American population, m



Origin of ancestry, %



Arab-Americans reassured by President Bush's conduct towards them, %



Sources: Census Bureau; Zogby International; Arab-American Institute

► common with a Yemeni Muslim fleeing persecution? Before September 11th, people like Mr Zogby (whose brother James is president of the AAII) were pushing to create an Arab-American lobby. The hope was that by showing their numbers in states like Michigan, California and New York, Arab-Americans could get more influence over everything from foreign policy to their generally negative depiction in Hollywood films. Now, suddenly, Arab-Americans find themselves being bundled together, but for the wrong reasons.

Meanwhile, the group is definitely changing—as the western Detroit suburbs of Livonia and Dearborn show. Livonia is a decidedly middle-class place. The new dome of St Mary's Antiochian Orthodox Church soars over well-tended, ranch-style homes. The large and prosperous Arab-Christian parish, founded three decades ago by Father George Shalhoub, has members of Syrian, Lebanese, Palestinian, Jordanian and Iraqi descent. Almost all of them were born in America, and many are successful professional types. Mr Bush's energy secretary, Spencer Abraham, is an occasional worshipper.

Livonia and suburbs like it may still be the norm: about 70% of Arab-Americans are Christian. But immigration is changing that. In Dearborn, only a 15-minute drive from Livonia, there are plenty of "boaters" (as local Arab teens call recent immigrants). These are largely Muslims from Lebanon, Iraq and Yemen. Women wear headscarves in the halal meat markets, kebab shops, and Arabic bookstores along Warren Avenue.

The town is home to eight mosques, with another huge one under construc-

tion. There are also several Islamic schools, which stick to the Michigan state curriculum but also offer daily Muslim prayer and Arabic-language training. In 1970, only 15% of immigrants from the Middle East were Muslim; in 2000, the figure was 73%, according to a recent study by the Washington-based Centre for Immigration Studies.

Many of the new arrivals are in bad shape. A local paediatrician points to cerebral palsy and developmental delays in the children of Iraqi refugees who were exposed to toxins when Saddam Hussein set oilfields ablaze in their country.

So there are differences, but there are also similarities—not just with Livonia but with all America's other immigrants. The Muslims in Dearborn are no less industrious than the Christians in Livonia: property prices have risen steadily over the past decade as the new immigrants have built up businesses. Zahid Bukhari, a political scientist at Georgetown University, is optimistic, arguing that Muslims are merely following other groups, such as Catholics, Jews, Japanese and even women, in being targeted. As a result, he says, "we are more determined to work in American civic life, to become more open."

For many Arab-Americans, this remains scant consolation. A group that imagined that it was growing out of a stereotype is now frightened and frustrated. In Livonia, Father George wrings his hands over his people's fate. "Someday, when I see God, I'm going to ask him why we need to be cursed this way," he says. "I hope he'll have an answer for me." ■

The Iraq debate

Fog of war

WASHINGTON, DC

President Bush says debate on Iraq can finally begin

FOR months, George Bush refused to join the "frenzy" about Iraq until he had decided what to do. Fair enough: until then, as he said, there is not much to debate. The trouble has been that everyone else has been leaping into the fray, with foreign leaders and a few Americans lining up to criticise military action.

This week, goaded by thus losing control of the debate, the president finally joined it. He promised leaders of Congress that he would ask for congressional approval, presumably for the use of force (the vote will probably come before election day on November 5th). He said he would consult the four other permanent members of the UN Security Council (inviting Britain's Tony Blair to Camp David this weekend). And he promised to lay out in

more detail his case for wanting to remove Saddam Hussein in a speech to the UN's General Assembly on September 12th.

Despite his keenness to remove Mr Hussein, the president does not seem to have chosen the means. That decision, he again insisted, had not yet been made. Rather, as Mr Bush told congressional leaders, "Today, the process starts." His comments bring forward the debate—and possibly the war.

They do so in a context somewhat more favourable to military intervention than seemed likely even a few weeks ago. Then, the administration was divided, even incoherent. In America, the commentary was led by sceptics. European and Arab critics were convinced the administration was preparing for unilateral war.

Nothing is quite so clear-cut now. It is true that divisions remain in the administration. The secretary of state has said the return of UN weapons inspectors is an essential first step towards ridding Iraq of weapons of mass destruction. Meanwhile, the vice-president has insisted the inspectors would merely provide "false comfort". But both could (just) be right. The inspectors may well be, as Dick Cheney said, pointless. But, because American allies might sign on to an attack only if they had been tried first, they might also be, as Colin Powell said, essential.

Next, the administration is still winning the battle at home. Most Americans say they support attacking Iraq anyway. Democratic congressional leaders left their meeting with Mr Bush sounding as if they might well back an authorisation of the use of force. It may be that the White House is offering Congress a deal: we will seek your approval and offer detailed explanations in exchange for a resolution that does not tie our hands.

Lastly, there may be some hope that America and its allies are not as divided as they sometimes seem. By saying he would consult the permanent Security-Council members, Mr Bush suggested he was still seeking an international coalition against Mr Hussein. And European foreign ministers are at least not rejecting that possibility. Last weekend, they met in Elsinore, Hamlet's castle. Instead of princely indecision ("Thus conscience doth make cowards of us all.../And enterprises of great pith and moment,/ With this regard their currents turn awry,/ And lose the name of action"), the Europeans agreed that the UN should give Iraq an ultimatum: let the inspectors back in, or else.

Anders Fogh Rasmussen, Denmark's prime minister, refused to say what the EU would do if Mr Hussein refuses. But it does seem as if Euro-opposition, at least at the government level, may be moderating a little. For a man who has yet to make his case with any conviction or force, Mr Bush is not in a bad position. ■

Homeland security (1)

A hole in the middle

WASHINGTON, DC

How much safer is America now?

GEORGE BUSH and the Democrats in Congress rejoined their battle this week over the mooted new Department of Homeland Security. The president wants the power to hire, fire and allocate workers in the name of flexibility. Democrats, who tend to be somewhat closer to the unions, accuse the Republicans of trampling on civil rights. They also want Congress to control the department's budget; Mr Bush wants to keep 5% under the discretion of the administration.

Which is all very well. But it seems to have remarkably little to do with making America safer. One year after America realised how vulnerable it was, it still does not have a department devoted to that project. What has been achieved?

The answer is a lot on the top and the bottom, and not so much in-between. On the international stage, America has improved safety dramatically by disrupting terrorist networks abroad. At the grass-roots level, a sudden awareness of risk has resulted in countless local safety reforms. But for everything in the middle—protecting hazardous waste, tracking foreigners, monitoring cargo ships and so on—improvements have so far been marginal.

That is less disastrous than it sounds: things like rebuilding disease-management systems require time. Moreover, the work abroad has helped. The terrorists arrested in places like France, Singapore and Morocco; the destruction of training camps; the fact that al-Qaeda's leaders are on the run: all these things have allowed for some breathing room to plan for better domestic safety.

The most dramatic area of improvement involves airlines and their passengers. The best reforms appear to have been the simplest ones, such as searching pas-

An unusually busy session for Congress

Lor', love a (lame) duck

WASHINGTON, DC

So many bills, so little time

CONGRESS gathers in New York this week to commemorate the anniversary of September 11th. It will be only the second time it has met outside Washington, DC, since its first session in the Capitol in 1800. Behind the commemorations, it also has a huge amount of work to do. No one expects it will get much done.

First on the list is trying to create the behemoth **Department of Homeland Security**. Next comes a measure to make it easier for people with 401(k) **pension plans** to sell holdings of their employer's shares. The House passed a version of this bill and, in the wake of the Enron affair, pensions reform is likely to sail through.

That cannot be said for five other bills, though all have passed both House and Senate. The chambers must now reconcile their differing versions before sending agreed bills to the president. They have managed to do this for a long-awaited reform of **bankruptcy law**, but the deal is being held up by foes of abortion: they object to a provision that would prevent abortion protesters who damage property from filing for bankruptcy in order to avoid paying fines.

The two chambers have started to reconcile different versions of the president's proposed **energy policy**. Agreement on this is also possible, but the White House will probably have to abandon plans to allow drilling in

Alaska's protected Arctic National Wildlife Refuge. A "**patients' bill of rights**" (allowing suits against health-maintenance providers) looks unlikely to get through. A bill to make the federal government the **insurer of last resort for terrorist acts** stands a chance. The only bill in conference that looks almost certain to pass is a measure to help states update clapped-out **voting equipment**.

Two much bigger measures, the overhaul of **welfare reform** and a proposal to expand Medicare to provide **prescription drugs** for old people (both passed by the House but not the Senate), seem likely to get lost in the rush of other business. For example: **Iraq** (the president has said he will ask Congress to approve the use of force); possible new **tax cuts** (which White House officials are talking about); and, last but not least, Congress's main job, the **budget**.

Partly because of disputes over the ballooning deficit, the House of Representatives has passed only five of the 13 spending bills which make up the annual budget. The Senate has passed just three. The budget is often late, but Congress has not been this late for ten years. In 1995, the inability of Bill Clinton and Congress to agree on a budget meant the government had to be shut down. No one expects that again. But many expect something almost as distasteful: a "lame-duck session", a meeting of the old Congress after the new one has been elected.

sengers more often and more thoroughly. Individuals paying more attention have also made a difference. The shoe-bomber, Richard Reid, was apprehended by flight attendants and passengers, not one of the new air-marshall police officers.

America's airline industry has now embraced security in a somewhat manic fashion.

The airlines already have to lock cockpit doors; soon they will install grenade-proof barriers that cost up to \$50,000 each. The federal government has offered to pay for 7,000 machines to scan baggage for explosives, three times as many as there currently are in the whole world. Altogether, the White House reckons that it will spend \$4.8 billion next year securing the skies (see chart). The deadline for these improvements may have to be extended for a year.

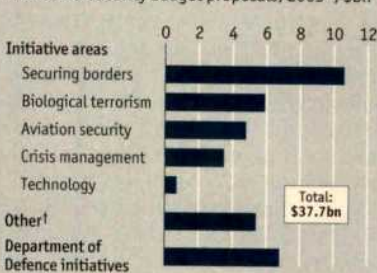
Many small neighbourhoods, cities and even states like Alaska (see story overleaf) have reacted a little like the airlines. John Thomasian of the National Governors Association argues that one of the main ways in which America's security has been enhanced is by putting many more guards at water reservoirs, power plants, bridges, tunnels and various pipelines. The National Guard has been particularly useful for this.

However, once homeland security ►►



An expensive shield

Homeland-security budget proposals, 2003*, \$bn



*Fiscal year ending Sept. 30th
 †Spending in federal departments
 Source: Brookings Institution

▶ starts involving co-operation between states or private groups, things get more patchy. Countless fairly simple reforms have been stalled.

Chemical factories, for instance, remain big targets: blowing one up could kill 10,000 people. Yet the task of protecting these unlit bombs has been left to the chemical industry itself, which, critics say, has done next to nothing. Peter Orszag of the Brookings Institution blames the president's reluctance to push the industry on Mr Bush's (sporadic) dislike of intervening in the private sector.

America's policy towards immigrant visas also needs clarification. Close to \$400m has been earmarked for a much-needed entry-exit visa tracking system; but a system to track students, which has been around for years, has been held up by political protests. Harsher controls may make for poor human-rights policy and even poor economic policy; but they are the best form of homeland security.

Planning for bioterrorism illustrates another problem: misallocation of resources. Plenty of money has been thrown at this: for instance, \$2.4 billion in federal grants will be doled out for laboratories and research on sophisticated surveillance systems next year. But only \$1.6 billion will go to what experts think may be the key to saving lives—upgrading public-health systems and regional hospitals, which are still in disarray. Similarly, America is spending \$650m building up a smallpox-vaccine stockpile. But many doctors may not be able to identify a smallpox victim, much less an Ebola-virus or plague victim. More training is desperately needed.

The cost of delay

In theory, the new homeland-security department will bring some order to all this. It marks the biggest government reorganisation since 1948: it will bring together some 170,000 workers from 22 government agencies. But the potential benefits of a one-stop shop for security already have to be weighed against the cost of reforms stalled during the construction.

The arrival of the new department has been an excuse for prevarication. Attempts to force some of the agencies to share information have been delayed until the workers find out whom they have to communicate with in the new structure. The Immigration and Naturalisation Service is waiting to see whether its service jobs (like visas) and security bits (like the Border Patrol) will be separated. The tiny amount of money being spent on technology reflects the fact that nobody is sure what sort of computers the new behemoth will need.

Bashing bureaucrats' heads together is the whole point of the new entity. Yet until it comes into being, the new department may be inadvertently making the homeland less secure. ■



Homeland security (2)

The chilling fields

JUNEAU

The view from the north-west frontier, along half of America's coastline

ALASKA a terrorist target? Most of the time, non-Alaskans tend to forget that the state exists. But in the frozen wastes of the far north-west, too, security has been ramped up. In all, some \$53m, almost all of it federal money, has been spent improving Alaska's defences. The state boasts its own Department of Homeland Security, albeit one with only three staff. None of this, alas, means it is secure.

Alaska's most important, and most vulnerable, resource is oil. The state supplies around 17% of America's domestically-produced oil, almost all of it channelled from fields in the north to the southern port of Valdez via the 800-mile Trans-Alaska Pipeline. Locals often take out their bad moods on the pipeline. Last October, a drunk closed it down for two days by shooting a hole in it, just one of more than 50 shooting attacks the pipeline has suffered in its 25-year history. A concerted assault by terrorists, especially one mounted in the depths of winter or at difficult-to-fix spots such as river-crossings, could seriously disrupt the country's oil supply.

Since September 11th, according to Major-General Phillip Oates of Alaska's Department for Military and Veterans Affairs, surveillance along the pipeline has increased, though he will not say by how

much. The state has also stockpiled extra equipment for making quick repairs. But Amory Lovins, an energy-security expert at the Rocky Mountain Institute in Colorado, says the pipeline is "indefensible" in its remotest parts. Worse, a serious winter attack could shut down the pipeline until the next summer at least, since the chilled oil would become gooey and hard to pump after a week of stagnation.

At Alaska's other sensitive spots—such as Fort Greely, about 100 miles from Fairbanks, where construction of a missile-defence interceptor is presently under way—security has also been tightened. But the toughest job may be guarding the coasts. Alaska has around half of America's coastline (yes, really), not to mention some of its most treacherous waters. Almost all goods arrive by ship. But the Coast Guard in Alaska is working on a shoestring, with just 2,000 people, including office staff. That represents a mere 4% of the agency's national manpower.

Over the past 12 months the agency has taken on all manner of new duties: instituting special homeland-security patrols; closing off part of the port of Valdez, the pipeline terminus; even reviving old radio networks to back up its Global Positioning System. Coast Guard crews must also keep a close watch on the cruise ships that meander up Alaska's coasts during the summer. All of this comes on top of ordinary peacetime duties, such as rescuing distressed boats, intercepting drug-smugglers and chasing off Russian fishermen who are forever trying to sneak across the maritime border to poach American fish.

Rear-Admiral James Underwood, the Juneau-based head of Alaska's Coast Guard, admits the agency is under strain, especially since it was able to muster few additional resources after September 11th: just 40 reservists, plus \$500,000 for extra equipment. Mr Underwood says that assimilating the national Coast Guard into the Department of Homeland Security (it is now part of the Department of Transportation) should improve its intelligence-gathering capabilities. But it is hard to imagine that a place as large as Alaska could ever be made completely safe. ■



Mid-term elections

Connecticut's idea of all-out war

NEW BRITAIN AND WATERBURY

What happens if two politicians agree on just about everything?

TO DAY-TRIPPERS from Manhattan, Connecticut is a Waspish land of well-guarded beaches, manicured lawns and soccer moms in luxury SUVs. Away from the "gold coast" of southern Fairfield County, however, these wealthy suburbs rub shoulders with decaying mill towns, farmland and rotting cities. With this spread of constituents in a small state, all but the most local of Connecticut's politicians understandably tread a careful middle line on most issues.

There are few better proponents of the art of moderate bipartisanship than Jim Maloney, a burly, personable, three-term Democratic congressman, and Nancy Johnson, a popular ten-term Republican. Awkwardly, thanks to redistricting, only one of them can now represent the state's congressional Fifth District. Both candidates have raised millions of dollars in campaign funds, and party leaders expect a good, dirty fight for one of the few really competitive House seats. The difficulty is finding something to fight about.

Mr Maloney, a bit more of a bruiser than the ladylike Ms Johnson, got off to the most promising start, with the discovery of Stanley Works, a local tool manufacturer whose shareholders had voted to reincorporate in Bermuda. The company had already shifted factory jobs overseas, depriving hardworking families of livelihoods in a suitably Enronesque manner.

Reincorporation, thundered Mr Maloney in July, was "unpatriotic and immoral in a time of war". He trumpeted a "Neal-Maloney bill", which would remove the tax incentive to incorporate offshore. And he pointed out that Ms Johnson, who lives in Stanley Works' home town, New Britain, had herself taken \$2,000 in contributions from one of the company's managers.

Briefly wrongfooted, Ms Johnson was, however, quick to deflect the idea that she was another Enronesque Republican. Far from hobnobbing with the corporate elite, her main connection to the company was her father-in-law, who worked there as a foreman. As for the Neal-Maloney bill, her staff claim that it should more accurately be called the "Neal-Maloney-Johnson bill", given her work drafting it. Meanwhile, Stanley Works has announced it is reconsidering its decision. So much for that yawning political chasm.

Mr Maloney started a new campaign at the end of last month in the car park of an

A new cathedral in Los Angeles

Not built by saints

LOS ANGELES

A fresh start for Roman Catholics, but recent wounds still fester

SUCCUMBING just a little to the sin of pride, the builders of the new Cathedral of Our Lady of the Angels in Los Angeles like to point out that, at 333 feet, it is 12 inches longer than St Patrick's in New York. LA is the biggest Roman Catholic archdiocese in America, with close to 5m members, 3m of them Spanish-speakers. The city's modernist cathedral, built in concrete with windows made of glowing slivers of alabaster, seems to stake a claim to leadership in a church that has been run for 150 years by Irish priests on the east coast.

The building, designed by Jose Mo-neo, a Spanish architect, was consecrated on September 2nd by Cardinal Roger Mahony, the archbishop of Los Angeles. The cathedral is part of a growing collection of grand civic buildings downtown, among them the Walt Disney concert hall—a characteristic flourish of gleaming stainless steel by Frank Gehry, a local architect—and the Dorothy Chandler pavilion, a former home of the Oscars. An "interfaith" service on September 4th expressed the city's hope that, suitably cushioned against earthquakes on its bed of shock-absorbers, it will serve as a spiritual rock for all citizens, non-Catholics included, to cling to. Some 6,200 people attended the two masses celebrated on September 3rd, the first day of regular services.

The Los Angeles Catholic Workers, a lay movement that organises soup kitchens in some of the grimmer streets nearby, gripes that the \$189.5m it cost could have been spent on feeding the hungry. The founder would not have approved, they grumble. Supporters point out that the old cathedral was damaged in the 1994 earthquake, and that the



Lights, camera, communion

money was raised specifically for the cathedral. But that only leads on to another bone of contention—the (wholly traditional) plan to give space in the expansive mausoleum beneath the nave to particularly generous donors.

Over all this, inevitably, hangs the cloud of paedophilia. Cardinal Mahony has generally been praised for taking a tougher line on errant priests than his east-coast peers. But an LA paper, the *New Times*, has still managed to identify several priests, accused of sexually molesting children in their charge, whom it claims the cardinal helped to protect from exposure. Earlier this summer, the cardinal apologised to his flock, in a letter read in every Catholic church in the archdiocese, for making poor decisions. This, more than any new cathedral, is the sort of thing that is needed to make Catholics feel good about their church.

abandoned Chinese restaurant in Waterbury, a struggling blue-collar city. "Oppose privatising Social Security", warned a freshly-erected billboard, carefully positioned to send a frisson of terror down the spines of passing elderly motorists. "There could not be a clearer, or more important difference between the two candidates," ventured Dick Gephardt, the House Democratic leader.

This was disingenuous, to say the least. As Mr Maloney went on to explain, what he actually opposes is a Republican suggestion that a small proportion of workers' Social Security contributions be invested in the risky stockmarket, where pay-outs cannot be guaranteed. He actually sup-

ported an earlier, less modest, "privatisation" proposal put forward by Bill Clinton. What is more, say Ms Johnson's people, she would only support investing Social Security funds in the stockmarket if payouts remained guaranteed, which is basically Mr Maloney's position.

And so it continues. Mr Maloney is in favour of abortion rights, but so is Ms Johnson. In the end, the election is likely to get decided the way elections usually are in Connecticut: on the candidates' personal ties and their record in sorting out local things like parks and hospitals. Ms Johnson's longer service may give her the edge. Whoever loses will be missed in Washington, but not for their radicalism. ■

Lexington A stubborn, patient man

The next few months will be crucial in defining the Bush presidency



GEORGE BUSH was not elected to face great challenges or bear great burdens. His appeal lay in his very lightness. He wanted to shrink the size of government, reduce the weight of taxes and disentangle America from unnecessary foreign involvement. People who wanted a busy government could vote for Al Gore. People who dreamed of national greatness and rolling back terrorist states could vote for John McCain. Mr Bush sold himself as a laid-back president for a laid-back nation.

How has this lightweight coped with one of the heaviest challenges a president has ever faced? Even Mr Bush's supporters concede that he got off to a lousy start. On September 11th, people looked to Rudolph Giuliani, or even to news anchors, for reassurance while their president zigzagged across the great blue yonder. But Mr Bush smartened up fast. In the disorientating days after the attacks, he succeeded in connecting with ordinary Americans—in feeling their grief without being mawkish and in expressing America's powerful sense of patriotism. He also made a notable effort to reach out to Arab-Americans, condemning racial stigmatisation, visiting mosques and inviting leading Muslims to the White House.

Abroad, the lampooned Texan cowboy, far from striking out blindly in a fit of rage and revenge, was methodical and patient, giving the Taliban every chance to surrender Osama bin Laden before launching military action and constructing an admirably broad coalition to do it. He also understood that the war on terrorism needed to be waged on many fronts at once, through espionage and diplomacy as much as warfare.

Part of Mr Bush's appeal in those first few months lay in the way he visibly grew in his job, finding a sense of purpose that had previously eluded him. One reason why this struck such a chord is that so many other Americans found themselves growing with him. Having voted for him because they took the same fundamentally lazy view of the presidency as he did, they shared his experience in the aftermath of September 11th too—first disorientation and then a realisation that they lived in a more serious world than they had ever imagined.

Most Americans would probably agree that Mr Bush put in a pretty impressive performance in the months after September 11th. The doubts come about his performance since the state-of-the-union address in January, in which he not only extended the

war to bring in the "axis of evil" but also repudiated his faith in a domestic platform of lower taxes and less government.

That domestic platform looks increasingly wobbly, not least because it has ignored the ramifications of September 11th. Mr Bush has left his policy of cutting taxes untouched despite the extra costs of the war on terrorism. His visceral suspicion of government significantly weakened the attempt to improve security at home. The administration wasted months fighting the creation of a Department of Homeland Security, only to give in to the inevitable at the eleventh hour. The suspicion remains that Mr Bush simply lacks the patience and energy necessary for the dull work of rearranging Washington's bureaucratic architecture. This is one area where a President Gore would have been far more successful than President Bush.

What about foreign policy? Here Mr Bush has certainly rethought his campaign strategy. Rather than withdrawing from the rest of the world, America is now as firmly involved with it as it has ever been. The president who preached a modest foreign policy is now the architect of a Bush doctrine that promises American activism for decades to come. Indeed, the questions all come from people who think that Mr Bush is biting off more than he can chew: that he is wrong to link the war on terrorism to the problem of rogue states; that he is allowing the question of Iraq to distract him from the more pressing issue of al-Qaeda; that he has backed Israel too unconditionally; that he is squandering international support and weakening an international coalition because of neoconservative blood lust.

Don't be deceived by the brush-clearing

The charge is accompanied by renewed doubts about Mr Bush's focus. In recent months Mr Bush has often reverted to his pre-September 11th persona: rather too listless and disengaged for comfort. He seems to have taken a back seat while rival factions in the White House slug it out, via speeches, articles and leaks, over how quickly America should act to eliminate Saddam Hussein. During Mr Bush's long holiday at his ranch in Texas last month, his administration seemed less like a modern government than a medieval court in which rival groups of courtiers were vying for the attention of a pleasure-loving prince (albeit one whose idea of pleasure is the decidedly unaristocratic pastime of brush-clearing).

The next few months will be as much of a test for Mr Bush as the first few months after September 11th. Has the president really been transformed by the attacks on the World Trade Centre and the Pentagon? Or is he returning to his idle old ways?

Given the relative paucity of information or action coming from the administration, nobody can answer this question definitively. But in one respect, at least, it would be foolish to underestimate Mr Bush: his will. The president may be a lazy man; but ever since winning the governorship of Texas he has built his political career on promising a few popular things, and then making sure that he does them (his big tax cut, for better or worse, illustrated this obstinacy). Now, with most Americans' blessing, he has said that he wants to remove Mr Hussein. Whether Mr Bush is going about it the right way is something his allies may query. But the fact that he is thinking about sending troops to Iraq over the objections of most of the world (and several distinguished members of his own party) suggests that September 11th has hardened a certain natural stubbornness in the president—and, perhaps, in his country. ■



Argentina's collapse

Carving up the scraps of power

BUENOS AIRES

President Eduardo Duhalde's authority to cut a deal with the IMF is seeping away, challenged by Congress and courts

FOR months, Eduardo Duhalde, Argentina's president, and his finance officials promised that an IMF deal was imminent. Recently, it seemed that this might even be true. But it has become clear that for every obstacle the government painstakingly surmounts, Argentina's Congress and its courts are capable of erecting another one. With a presidential election not due until March, and with no convincing candidates emerging, the prospect of Argentina recovering from its shocking economic collapse seems to recede like a mirage on an endless Pampas road.

The government is still going through the motions of trying to reach an agreement with the IMF which would at least roll over Argentina's obligations to the Fund itself. This week yet another IMF mission was in Buenos Aires. Roberto Lavagna, the economy minister, earlier made great play of writing his own draft letter of intent (though such documents are normally quietly negotiated). But the IMF dashed his hopes. "In the monetary area and the banking area and some aspects of the legal side, clearly there are issues remaining," the Fund's spokesman, Thomas Dawson, said last week. He added that the two sides were not "talking about any kind of final timetable" for a deal.

The government thinks this unfair. The economy seems to have stopped shrinking at last. Since June, the peso has hovered close to 3.60 to the dollar. Although that is

a devaluation of 72% since January, inflation remains restrained. The central bank's reserves have risen a little. So have tax revenues. The central government had a budget surplus of 200m pesos in July, though that would disappear if Argentina resumed debt payments. Moreover, with financial turbulence spreading to Uruguay and Brazil (both of which promptly received IMF bail-outs), the case for helping Argentina seemed to be stronger.

But the government has yet to show that it has a coherent economic programme. In particular, it has not decided what to do about bank deposits frozen by a previous government last December. Congress, having blocked a plan to turn these into bonds, has turned its attention to bank bashing. The average Argentine still blames the banks for the confiscation of savings (though this was decreed by the government) and much else besides. The banks, in turn, having written off huge losses, want reassurance that Argentines still want a banking system.

Congress recently extended for three months a ban on mortgage foreclosures and the seizing of debtors' cars. The Senate unanimously approved a bill reinstating a 2% tax on interest and commissions for a bankrupt trade-union health scheme. (At least one banker is reported to have been told that this measure could be scrapped—for a fee). Another measure would make foreign banks' head offices liable for new

deposits in their Argentine branches. Until such measures are withdrawn, the banks want any deal with the IMF halted. But they have agreed with the government to delay indexing most loans to inflation.

Then there are the courts. On taking office in January, Mr Duhalde misguidedly set in motion the impeachment of the Supreme Court. But having failed to raise the necessary two-thirds majority in Congress, he is now desperately lobbying to halt this because the court is bloodily-mindedly ruling government measures unconstitutional. Last month, it struck down a 13% cut in government salaries and pensions made last year. That creates a large fiscal hole. The court may also reverse a government decree which converted dollar deposits into pesos. That would mark the end of the banking system, whose dollar-denominated assets were turned into (devalued) pesos at par.

The creeping paralysis of government has led to calls for the presidential election to be brought forward. But the candidacy of the ruling Peronist party is being squabbled over by half a dozen contenders. None are impressive. Leading the polls, but with less than 20%, is Adolfo Rodríguez Saa, who as interim president in December declared the debt default, and was previously the satrap of the western province of San Luis for 18 years.

Argentines are clamouring for new leaders. But none has yet appeared. Increasingly, authority is slipping back to the provinces, where it belonged for the first chaotic half-century of the country's independent life. The danger Argentina faces is one of stasis, in which the election fails to produce a government capable of imposing its will, or of starting to rebuild the country's discredited institutions. No wonder that the IMF is now demanding "political consensus" for any deal. ■

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Uruguay's economy

Panic over, depression not

MONTEVIDEO

A long struggle with recession, inflation and debt lies ahead

URUGUAY'S customary tranquillity has started to return since the IMF and other international bodies came to this small South American country's rescue last month with a \$3.8 billion bundle of loans. A stampede to pull deposits out of the banks, which forced the government to declare a four-day bank holiday in early August, has stopped. There has been no repeat of the looting seen at the same time in Montevideo, the capital. A big protest march organised by the trade unions last week passed off without violence.

But while the immediate panic has died down, Uruguay now faces a long, hard battle against economic depression and crippling public debt. The government predicts that the economy will shrink by 11% this year and a further 4.5% in 2003—which will be the country's fifth successive year of recession. Inflation is expected to be 40% this year and 50% next. Unemployment has climbed to 16.7%.

Even so, the IMF money has injected a veneer of confidence. Uruguay's bonds have recouped some of their steep losses. While Argentines, whose savings back home are still blocked, continue to withdraw cash from their Uruguayan accounts, local customers have been putting money back in. Many savers in four troubled private banks temporarily shut by the government have accepted a plan under which 30% of their deposits would be swapped for bonds. But it is proving hard to persuade shareholders, or new investors, to stump up enough extra capital to allow these banks to re-open. So far, only the Moonies, a religious sect which owns a stake in one of these banks, Banco de Credito, have offered fresh money.

Almost all of Uruguay's public debt of

\$10 billion is in dollars. Since the peso has devalued by 50% this year, and remains weak, the debt burden has soared, to almost 100% of GDP. That is forcing the government to seek drastic spending cuts, and some tax rises, to avoid a debt default. This week, Montevideo's main public hospital cancelled all non-urgent operations for the rest of the year. Three of Uruguay's foreign embassies are to close. Payments to government suppliers have been halted, to ensure that at least salaries and pensions will be honoured. Even congressmen have been told they will have to supply their own coffee and toilet paper.

This austerity will test Uruguay's political consensus. President Jorge Batlle has a majority in Congress, so he should gain approval for next year's tough budget. But in the streets, says Adolfo Garce, a political scientist at the University of the Republic in Montevideo, several groups, such as truckers and civil servants, are planning protests to press for handouts to compensate for rising prices. The left-wing opposition, the Broad Front, already looking ahead to a presidential election due in 2004, reckons (wrongly, thinks Mr Garce) that its best tactic is to radicalise. Its leaders recently decided to put themselves at the head of any future protest marches, and issued a list of spending demands.

Faced with such pressures, Mr Batlle's "solution" will be to print money, says Ernesto Talvi, an economist at Ceres, a think-tank. The resulting inflation will bump up tax revenues, while reducing the value of spending, thus leaving enough money to service the debt. But this is risky: inflation will weaken the peso, thereby increasing the debt. And Uruguayans, especially the poorest ones, will suffer a further fall in living standards.

Whether Mr Batlle can avoid a default depends in part on how much social unrest he faces. Some analysts, including Senator Danilo Astori, the Broad Front's most moderate congressman, fear that the opposition's radicals will whip up enough protests and strikes to force Mr Batlle to abandon austerity, in the hope that this would increase the opposition's election chances. However, voters might punish the opposition if they blamed it, rather than Mr Batlle's centre-right alliance, for the economic chaos that a default would bring. But it is unclear how good the opposition is at judging what is in its own electoral interests, says Mr Garce.

Uruguay's fate also depends on the wider world, and especially on its two big neighbours. An end to financial panic, and a return to growth, in Brazil would help. So would a resolution of Argentina's banking morass. And a livelier world economy would lift the prices of Uruguay's farm exports. At best, Uruguay faces a long, hard slog before it recovers its reputation as South America's Switzerland. ■

Drugs in Colombia

The weedkiller war

BOGOTA

A big new effort to repress the cocaine industry



LAST year, some 35,000 peasant farmers in the Colombian department of Putumayo, the world's largest single source of cocaine, signed pacts agreeing to pull up their coca bushes within 12 months in return for government aid. Thousands complied; many more did not—not least because aid was slow to arrive. Now Colombia's new government, supported by the United States, is all but scrapping this policy of voluntary eradication in favour of a big new push to spray coca fields with herbicide. After a decade in which coca production steadily rose in Colombia, American officials say that this year they will finally start to get on top of it.

Alvaro Uribe, who took office as Colombia's president a month ago, has made containing the country's guerrillas his top priority. The United States Congress recently approved an administration request to allow American military aid, previously targeted against the drug trade, to be used against the insurgents. But officials from both countries insist that fighting drugs is an integral part of tackling the illegal armies (of right-wing paramilitaries as well as left-wing guerrillas) which profit from and protect the cocaine trade.

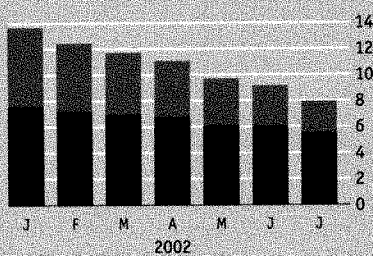
That was the logic of Plan Colombia, a scheme backed with \$1.3 billion in American aid in 2000. Only now are its full effects starting to be felt: extra crop-dusting aircraft (to spray coca fields), and helicopters to protect them and to destroy drug-processing labs, are arriving. Since July 28th, they have sprayed 20,000 hectares (49,400 acres) of coca in Putumayo. That compares with just 5,000 hectares eradicated voluntarily.

Even before the latest spraying campaign, there were some signs that coca out- ➤

Foreign flight

Uruguay's banking system:
foreign-currency deposits, \$bn

■ residents ■ non-residents



Source: Banco Central del Uruguay

put in Colombia was declining. Last November, the latest annual survey by the UN Drug Control Programme found that the coca crop had fallen by 11%, to 145,000 hectares. American officials reported a slight fall in the purity of Colombian cocaine. But Klaus Nyholm, the UNDCP's man in Colombia, says he has "more than a hunch" that the productivity of the country's coca fields has risen over the past five years, meaning that more cocaine could be coming from fewer hectares.

Andres Pastrana, Mr Uribe's predecessor, was reluctant to authorise all-out spraying. He feared that this would prejudice abortive peace talks with the FARC, the main guerrilla group, which controls much of Putumayo and neighbouring Caquetá. And critics say that spraying damages human health and the environment—as well as wiping out adjacent food crops. Officials counter that glyphosate, the herbicide involved, is harmless to health, and that the coca industry itself does huge ecological damage. Under Mr Pastrana, only commercial coca plantations, of three hectares or more, rather than family farms were supposed to be sprayed. Now there have been reports that this restriction has been dropped.

Although some of his advisers are said to be nervous about driving more coca farmers into the ranks of the FARC, Mr Uribe insists that spraying is needed. "If we don't destroy drugs, they will destroy our democracy and ecology", he says. On September 3rd, he issued a decree speeding up the procedure for confiscating drug traffickers' assets. He is also keen on shooting down drug planes. According to Francisco Santos, the vice-president, a score of clandestine flights each week carry drugs to Venezuela, returning with arms. Such aircraft were routinely intercepted, with CIA help, until an incident last year in which an American missionary and her baby were killed when their plane was shot down in Peru. American officials say

Politics in Guyana

Tinderbox

PORT OF SPAIN

The fear of racial violence

ON AUGUST 30th, Rasta chants and a march with the national flag marked the funeral of Andrew Douglas, a gangster killed in a gun battle with police. The fact that Mr Douglas was a national celebrity says much about Guyana's problems. A former policeman, he escaped from prison while awaiting trial for five murders. He then popped up on television, in army fatigues and with an AK-47, calling himself a freedom fighter. "Look into innocent black Guyanese problems or unrest will not finish," he said.

What followed was a crime wave with racial overtones. Since February, eight policemen have been killed. The latest victim was Vibert Inniss, deputy head of the customs anti-narcotics unit, shot last month as he stopped to buy a newspaper in Buxton, the centre of much of the violence. The gangsters seem to be mainly Afro-Guyanese. Indo-Guyanese, who make up 48% of the population, feel targeted, and plan their movements carefully.

Guyanese politics, too, is uneasily split along racial lines. In July, two peo-

ple were killed and ten were injured when protesters stormed the office of the president, Bharrat Jagdeo, during a meeting of Caribbean leaders. The mainly Afro-Guyanese People's National Congress, the main opposition, is ambivalent towards the violence, which it blames on youth unemployment, police brutality and corruption.

Several times in recent years, Guyana has seemed on the brink of widespread racial violence. So it looks once again. For five years, the economy has stagnated. Repeated attempts by Caribbean leaders, foreign diplomats and local mediators to get the two main parties talking have had limited success. The PNC ended the most recent dialogue in April.

Two attempts to re-start the talks are in progress. One is led by a Commonwealth representative, Sir Paul Reeves, a former governor-general of New Zealand. Meanwhile, the private business lobby, the trade unions and the local Bar Association have called a carefully-prepared meeting of all political parties for September 11th. The choice of date might just command some respect.

they will soon authorise the resumption of the shoot-down programme.

As for providing coca farmers with alternatives, Mr Uribe says he supports "practical" projects, such as forestry. Few legal crops flourish in Putumayo, which is remote and has poor soils. Mr Uribe is due to travel to Europe this month to seek \$300m in foreign aid to help 50,000 peasant families, two-thirds of them in Putumayo. But European governments, while

criticising spraying, have not reached into their pockets to back the alternatives they claim to favour. Out of \$113m pledged since 1996 to Plante, the Colombian agency for alternative development, \$104m has come from the United States.

Opponents of spraying argue for a more patient approach. "You can spray a field in five minutes, but development takes more like five years," says Mr Nyholm. "When you spray, often the farmer replants coca, either on the same field or further into the forest." Putumayo's governor, Ivan Guerrero, says that voluntary eradication, and Mr Pastrana's investment in roads and health posts in the area, led residents of his long-neglected department "to believe in the state again". He hopes farmers will voluntarily rip up a further 5,000 hectares by the end of the year.

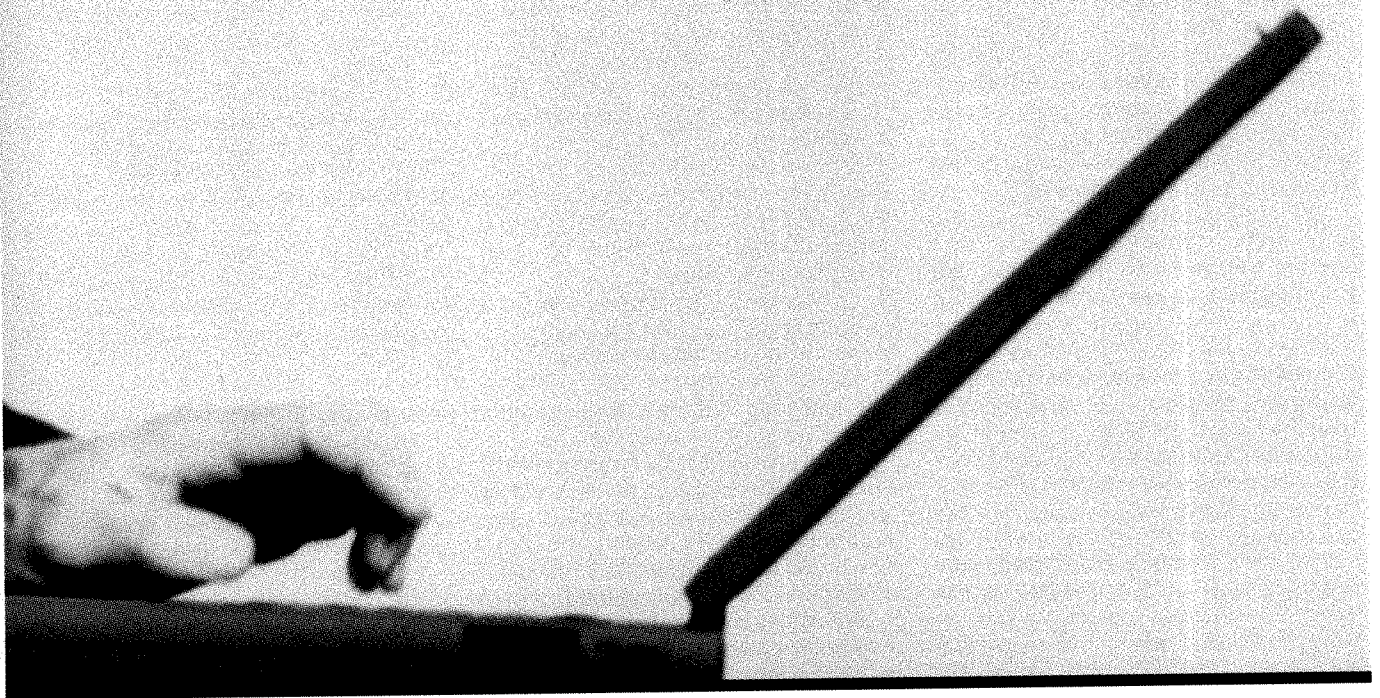
But under the new policy, officials hope to spray 121,000 hectares this year, up from 94,000 hectares last year—and faster than the rate of replanting, they claim. Whether that will hurt the FARC, and the other armed groups, more than it helps them, remains to be seen. And even if the Colombian coca crop falls significantly, all the signs are that Peru and Bolivia will take up the slack. Even if the Andean drug war has indeed entered a new phase, it is nowhere near over. ■



If only they were fertilising food crops

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Famine in Ethiopia

Drought, death and taxes

ASSAITA

Six million Ethiopians are going hungry. The weather, and a war, are to blame

A GREAT lake stretches across the desert, shimmering enticingly. Unfortunately, it is a mirage. The Afar region of Ethiopia, perhaps the hottest inhabited place on earth, is even drier than usual this year, and the people who live there have run out of food. Their beloved cows lie dead and dying in the hot sand. Many of the carcasses are so fresh that the storks and hyenas have not yet had time to peck or chew them clean.

In much of eastern, southern and northern Ethiopia, the rains have been rotten this year. In all, 5.9m of Ethiopia's 65m people need food aid or other assistance, according to the World Food Programme. The food shortage is not as terrible as the one in southern Africa. Nor is it as disastrous as the famine Ethiopia suffered in the mid-1980s. Ethiopia's current government is not indifferent to human suffering in the way its old Marxist dictatorship was, or Zimbabwe's government now is.

Nonetheless the situation is grim. Among the worst affected are the Afars, a tough, gun-toting people who subsist by herding livestock in the arid vastness of north-eastern Ethiopia. The Afars are almost all poor, but like most pastoralists, they have developed sophisticated methods for avoiding starvation. Their only assets are their animals, but they diversify their portfolios, so to speak, by breeding cows, goats, camels and sheep. Cows are a

high-risk, high-yield investment. They breed fast and produce lots of milk, but they are the first beasts to die in a drought. Goats are scrawnier, but hardier. Camels are the toughest of all, but breed slowly. Afars have insurance, too, in their kinship ties. In hard times, those with spare livestock share with those who have not.

Despite all these precautions, Afars are often malnourished. Their nomadic traditions fiercely discourage them from settling down, but many have grown desperate enough to start rearing maize as well as cows and camels. Most years, these "agropastoralists" have enough to eat, but this year even they are suffering.

"All our cows died, and the ground is too dry to grow maize," says Muhammad Oumar, a skinny father of four, squatting in the dust by a tree of yellow orioles. Hunger has not yet turned to starvation in his village; the villagers hike 20km (12 miles) to Assaita, the nearest town, to sell woven mats or firewood and buy flour. But there is not enough to go around, and malnutrition has made many vulnerable to disease.

Children have no milk, and must make do instead with a thin porridge made from teff, an indigenous grain. The 15 households in Mr Oumar's village look after 20 orphans between them. In another nearby village of 100 homes, 13 people have perished in the past month, according to Mu-

hammad Hassan, a peasant with sunken, cavernous cheeks. "We need food," he says, "or we're going to die."

The immediate cause of Ethiopia's food crisis is the weather. But political factors play a role, too. After Ethiopians shook off their Marxist overlords in 1991, food production rose steadily. But between 1998 and 2000, a pointless war with neighbouring Eritrea stymied progress.

Strong young men were summoned from their fields and sent to the front line. Tens of thousands of people were killed, and perhaps 350,000 forced to flee their homes. Families with members on both sides of the border were separated. Flour mills, bridges, power lines and irrigation systems were destroyed. Most aid was frozen. In all, the war cost Ethiopia \$2.9 billion, according to the Ethiopian Economic Policy Research Institute, a private think-tank. That is almost a whole year's output for every farmer in Ethiopia; and more than 80% of the population live on farms.

Wanted: rain, aid and tax cuts

Another problem, strangely, is tax. Ethiopia abandoned feudalism in the 1970s, when the emperor, Haile Selassie, was murdered, but the old feudal habit of taxing peasants persists. The most irksome levy is payable on the land that peasants till, which they are not allowed to own, because the government owns all the land. The sums involved are small, but do not seem so to those who pay them. Mr Oumar usually hands over 60 birr (\$7) a year, which he describes as "heavy". The average Ethiopian income is only \$100 a year, but most peasants earn far less.

Tax-collectors generally make an exception for those who are on the verge of starving: this year, Mr Oumar was let off. They tend not to tax nomads either, partly ►►

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▶ because they are hard to trace, and partly because so many carry submachineguns. But taxes levied on peasants in years when the harvest is good make it hard for them to accumulate a surplus to see them through the bad years.

What is more, taxes must be paid in cash, shortly after harvest time. To raise this cash, peasants all take their spare crops to market at the same time, which depresses prices and means they have to sell more of their crop to meet their tax bill. The tax raises negligible sums for the government (only 1% of total annual revenues), but inflicts serious harm on the most vulnerable Ethiopians. "If we don't pay," laments Mr Oumar, "they say they'll take our land." ■

Islamic law in Nigeria

The attractions of sharia

KADUNA

Nigeria's sharia courts are harsh, but quicker and cleaner than secular ones

PUBLIC executions make an ugly backdrop to a beauty contest. Nigeria will be host to the Miss World pageant in November, but several beauty queens have threatened a boycott in protest at the Islamic courts in northern Nigeria which have recently condemned four people to be stoned to death. One young woman, Amina Lawal, was condemned for having been made pregnant by a man who, she says, promised to marry her, but didn't. (Her alleged lover was acquitted.) None of the stonings has yet been carried out, but the controversy around Islamic law, or *sharia*, threatens to destabilise Africa's most populous nation.

Over the past two years, 12 predominantly Muslim states in northern Nigeria have adopted versions of *sharia* for criminal cases. Nobody minded when Muslims used *sharia* to solve land disputes and family squabbles, but the introduction of penalties such as flogging (for drinking alcohol), amputation (for theft) and stoning (for adultery) has outraged non-Muslims, sparked sectarian riots in which more than 3,000 people have died, and cast doubt on the central government's ability to uphold Nigeria's secular constitution.

However, most of Nigeria's Muslims applaud the imposition of *sharia*. This is partly because they believe it reflects the will of God, partly because Nigeria's secular courts are so awful. A former British colony, Nigeria inherited a judicial system based on English common law. Trials involve expensive lawyers, fussy procedures and lots of paperwork. The system is cumbersome and underfunded.

In crumbling courtrooms, judges take evidence in long-hand, court records are typed up on ancient manual typewriters, and law books are in short supply. Underpaid policemen, and judges too, often accept bribes to pervert the course of justice. According to Human Rights Monitor, a lobbying group, most inmates in Nigerian prisons are still awaiting trial. Many languish behind bars because their case files have been lost. Judges visiting congested prisons often release inmates because they have already served the maximum sentence allowable for the crime of which they have not yet been convicted.

In *sharia* courts, by contrast, disputes are settled without strict adherence to written rules of procedure. Cases are judged according to local customs and Islamic beliefs. Most people choose to represent themselves, which saves legal fees. The resultant justice may be rough, but it is quick. While it can take months just to get a hearing in a regular court, parties can get a hearing the same day in a *sharia* court, simply by showing up. Even Nigeria's justice minister, Kanu Agabi, admits that in *sharia* courts, "if a man owes you money, you can get paid in the evening. Whereas in the regular courts, you can sit in court for ten years and get no justice."

The current dispute over *sharia* began in 1999, after a southern Christian, Olusegun Obasanjo, was elected Nigeria's president. His victory upset some Muslims, who had grown accustomed to seeing their co-religionists in the presidential palace. Almost immediately, northern states started extending *sharia* to criminal cases as well as civil ones. Its supporters argue that harsh punishments deter violent crime. But Christian leaders take a more cynical view: they argue that northern

politicians are using *sharia* to consolidate their power base.

Mr Obasanjo, who wants to avoid more religious riots, and is also anxious not to offend certain powerful northern generals, has so far looked the other way. But he may soon have to take a stand. Ms Lawal's case is making its way through the appeals process and could soon end up before the Supreme Court, which may rule the *sharia* penal code unconstitutional (as the government has already said it is). Such a ruling should save Ms Lawal, but big trouble could follow. ■

Iranian reform and anti-reform

Crushing the reformist pillars

TEHRAN

Having bashed the press and students, the conservatives threaten parliament

"I ACCEPT that there is a sort of hopelessness in our society," admits Iran's reform-minded, and thus serially frustrated, president. At a press conference last week, Muhammad Khatami started to fight back at the conservatives who sap his authority. He would, he said, soon be presenting a bill that might better enable him to carry out his duties. But will it? Probably not, so long as the conservative establishment, led by Iran's supreme leader, Ayatollah Ali Khamenei—the "unelected few" in George Bush's words—retains its blocking power, and its hold on the judiciary.

Four obstacles stand between those unelected few and their outright victory: the Iranian people who have twice decisively voted Mr Khatami into power, the reform-dominated parliament, the reformist press and a bunch of brave young students. The judiciary crushed the student movement months ago. Now it has completed its elimination of the reform-minded press. It recently upheld the ban on *Norooz*, the last outspoken newspaper, and stopped two new ones from filling the void. Well over 70 papers, new and old, have been closed in the past three years.

So that leaves parliament and the people. But there is doubt how much stomach either have for a fight. Prison sentences are handed out freely. In July, 33 liberal politicians were sentenced to jail. None was a deputy, but Mohsen Mirdamadi, the managing director of *Norooz*, has been sentenced to six months in violation of his immunity as head of parliament's national security commission.

Parliament is in two minds. Last month, in an open letter that deplored the judges' "premeditated" verdicts, more than 150 reformist deputies wondered if there was anything, besides "seeking refuge in God", ▶



When she is weaned, her mother dies

► that could be done. These parliamentarians have a well-founded suspicion that the Council of Guardians, an appointed upper house that vets laws and parliamentary candidates, intends to disqualify dozens of them from seeking re-election in 2004. If that happens, they will lose even the less-than-reliable protection afforded them by parliamentary immunity, and will be easy prey for public prosecutors.

Last weekend, parliament gave the finishing touches to a bill which, if passed, would deny the Council of Guardians their right to disqualify electoral candidates. But the council itself may shoot this down. If so, more and more deputies may take the view that their only course of action is to resign. But refusing to co-operate has a price. The Revolutionary Guard has uttered warnings against actions injurious to "national morale". The head of the judiciary has indirectly accused reformist deputies of "the biggest betrayal of Islam, the revolution and the people."

Ah, the people; they are easily forgotten as the elite fiddles. Mr Bush latched on to demonstrations in July as evidence of popular mobilisation. They were nothing of the sort. Their tiny size, and the disproportionate brutality with which they were put down, came as a reminder that Iraqis have rarely been so sullenly apathetic, or the forces of suppression so strong. ■

End of a bit of history

The 5,000-year-old way of life of the Marsh Arabs, celebrated by Wilfred Thesiger among others, has long been under threat. Its final disappearance is documented in "The Iraqi Marshlands" edited by Emma Nicholson and Peter Clark, and published this week by Politico's. As the map below suggests, Saddam Hussein's aggressive drainage programme in the 1990s, which had the dual purpose of reclaiming land and pursuing rebels hiding in the waterways, turned much of the marshland into desert, depopulating the area. Some 200,000 of the inhabitants fled, many of them to refugee camps in Iran. The damage is probably irretrievable.



Egypt's political scandals

Gamal, the brisk new broom

CAIRO

With the old guard in trouble, Mubarak's son may lead in the new

POLITICS is rarely exciting in a country where one party and one president have ruled unperturbed for two decades. But a recent spate of scandals and a looming shake-up of Hosni Mubarak's National Democratic Party (NDP) are stirring Egyptians out of their conditioned torpor.

It is not that scandals are new to Egypt. Cairo's gloriously rabid gutter press regularly feeds on the carcasses of officials dislodged from the country's 6m-strong bureaucracy. Usually, the sacrificial victims are ex-ministers, or mid-ranking officials at a safe remove from real centres of power. Lately, the spotlight has shifted perilously close to stalwarts of the regime.

The presidency itself is, by Egyptian tradition, untouchable. So, too, has been a triumvirate of ageing ministers who have held their cabinet posts, and top commands in the party, almost as long as Mr Mubarak. In the past two months, however, prominent associates of all three have come under investigation.

The most recent exposé concerns an undersecretary in the Ministry of Agriculture, who police say was taped accepting a \$3m bribe from a French firm to import its pesticides. Subsequent leaks unleashed a torrent of further charges, ranging from adultery to poisoning unsuspecting peasants with toxic chemicals to, horrors, consorting with Israelis.

Being alert to media excess, Egyptians were less surprised by the accusations than by the fact that the official had long been a right-hand man to Youssef Wali, who has been minister of agriculture, deputy prime minister and secretary-general of the NDP since the early 1980s. Mr Wali had vastly broadened the powers of his protégé, appointing him to more than 30 posts inside his sprawling empire.

Earlier this summer, Cairo's fraud squad had nabbed another powerful undersecretary, this time in the Ministry of Information. Muhammad Wakil, who was director of news for Egypt's ponderous state television monopoly, was caught taking a bribe to put a prominent doctor on a popular chat show. For 20 years the ministry has been the fief of Safwat Sherif, who also happens to be the NDP's deputy secretary-general. The minister was not directly implicated in the scandal. What hurt him were subsequent revelations that the man he had entrusted to dispense the country's carefully circumscribed news diet had been charging "clients" for years.



His father's heir?

The third scandal, involving an investigation into banking fraud, touched a close associate of the minister for parliamentary affairs, Kamal Shazli. The minister is the NDP's chief whip, with a reputation for tough back-room dealing.

Taken separately, none of these cases would have raised an eyebrow. The opacity, complexity and sheer size of the Egyptian state have long encouraged graft. Similarly, the vast patronage network that has ensured the NDP a stranglehold on power—it has never scored less than 70% in a general election, and currently holds an 86% parliamentary majority—has also opened opportunities for self-enrichment. Corruption, Egyptians are fond of saying, is so endemic that the country would come to a stop without it.

What has set Cairo's rumour mills turning is the fact that these latest scandals coincide with attempts to reform the NDP from within. Leading these efforts, since his appointment to the party's 25-member secretariat two years ago, is Mr Mubarak's son, Gamal. With the president having declared that new blood is needed in the party, and with a rare NDP conference scheduled to be held next week, Egypt's media keenly speculate that a purge of the party's top ranks is in prospect.

The wilder talk is of the younger Mubarak ousting the NDP's old guard as part of a careful process to legitimise him as the heir to the presidency. But nothing in Egypt is quite what it seems. There has certainly been internal party resistance to 39-year-old Gamal Mubarak's quiet rise. His father, however, has always been careful to build a consensus within the ruling circle before making any move. And the old guard have survived so long for a good reason: loyalty to the chief. ■



Europe Must Improve its Pharmaceutical Competitiveness

by **Fabio Pammolli**

Pharmaceuticals have long been a strategic economic sector for Europe. They have contributed greatly to the continent's balance of trade in high-technology, research-intensive fields. In recent years, however, Europe's pharmaceutical sector has come under considerable pressure. In a recent study, several colleagues and I found that European pharmaceutical firms have become less competitive vis-à-vis U.S. companies, and are losing ground in terms of innovative capabilities and performance.

Reversing a previous trend, Europe's pharmaceutical market grew more slowly than the U.S. market throughout the 1990s. This relative decline resulted from a slowdown in Europe's own market growth and an increase in U.S. growth. American pharmaceutical firms rely heavily on high-tech, non-labour inputs, while those in Europe are far more labour-intensive. Investment in pharmaceutical R&D fuelled U.S. market expansion throughout the '90s, while Europe's pharmaceutical-sector growth depended on factors other than R&D, capital, or labour. In other words, capital and R&D investment in Europe has translated less markedly into sales growth.

When we compare new-product sales of leading pharmaceutical firms in Europe and the United States, we find that sales by U.S. multinationals grew far more rapidly than those of European multinationals, even though companies in both markets discovered and developed equivalent numbers of new medicines. Among the explanations for Europe's relative sales weakness are, first, a growing U.S. advantage in sales generated by new medicines, and second, a trend towards relative obsolescence in European corporate drug portfolios.

During the 1990s, the United States supplanted Europe as the seat of pharmaceutical innovation. This is, in part, because the United

A world of ideas on public policy.

States fostered a division of labour between smaller biotech companies specialising in drug discovery and larger firms adept at commercialising new products. The U.S. comparative advantage is also evident in the greater use by U.S. firms of new drug development tools such as genomics and high-throughput screening. Because European companies have been content to rely on technological advances generated by U.S. firms, they have forfeited a critical source of growth.

EU member-state governments should guarantee and enforce strong patent protection for innovative medicines, and... avoid over-regulating pharmaceutical markets in ways that restrict patient access and discourage innovative research

Specific regulatory frameworks have exacerbated the lack of competition in some European pharmaceutical markets, causing greater inefficiency. Some countries – especially those that have adopted administered drug-pricing systems in order to protect marginal local companies – have seen no significant fluctuation in prices or market share, both of which would normally decline as patents expire and generics enter the market.

Europe's pharmaceutical sector must address its relative disadvantage in technological innovation vis-à-vis the United States. To excel in this area, Europe must upgrade its research base to ensure that its scientists have a solid biomedical educational and research infrastructure. Although extremely high-level research communities exist at the national level, they are fragmented, frequently

small-scale, and often cosseted by state protection. Integration of labour markets for researchers and competition among research units in a system based on peer-review constitute an important component of this process.

Without question, Europe's pharmaceutical sector needs an integrated research infrastructure, as well as more links with university-based researchers. Greater collaboration among Europe's public research institutions and private firms would boost research productivity, without minute segmentation of development efforts.

Europe can most effectively boost its competitiveness by abandoning protectionist pricing and marketing strategies that discourage pharmaceutical innovation. European Union (EU) member-state governments should guarantee and enforce strong patent protection for innovative medicines, and their national health authorities should avoid over-regulating pharmaceutical markets in ways that restrict patient access and discourage innovative research. In particular, EU countries should foster a wider variety of mechanisms and sources for financing healthcare and pharmaceuticals, and they should adopt more open formularies as a way to spur market competition.

Movement towards a more market-based regulatory environment will become even more important as the EU expands to include Central and East European countries. If enlargement takes place within a market-oriented context, it can help to make Europe's pharmaceutical sector more globally competitive. If not, enlargement might simply aggravate the existing distortions.

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Germany's election

Watch your step

MUNICH

What kind of chancellor would Edmund Stoiber be?

WITH barely a fortnight to go before the general election, the ruling Social Democrats, who have been lagging well behind for most of the past eight months, are now running neck and neck with the centre-right Christian Democrats. And Edmund Stoiber, the conservatives' candidate for chancellor, is beginning to lose some of his cool. After being pelted with eggs and tomatoes in Leipzig and jeered in Cottbus, he must have been relieved to be among friends at a conservative party rally in Dusseldorf last weekend. But as he strode triumphantly up to the stage amid dancing laser beams, pounding rock music and rapturous applause, he stumbled, falling flat on his face.

Was this an omen, many wondered? For the first time, one poll puts the Social Democrats and the Christian Democrats both at 39%, although according to most polls the conservatives still have a slight lead. The liberals, their likely partners, are forecast to get 7-9%; the Greens, the Social Democrats' preferred allies, 6-7%. With these results, neither camp could expect to command an absolute majority in parliament. But if the ex-communist Democratic Socialists fail to get the minimum 5% required to get them back into parliament, the party with the most votes, currently the conservatives, together with their liberal allies, would be assured of a parliamentary majority. Mr Stoiber would

then become chancellor.

What kind of chancellor? From his programme, described by one of his potential liberal allies as "gutless and flabby", it is difficult to judge. Though he has been depicted by his opponents as an arch-conservative, he puts himself firmly in the middle ground. On the economic front, he is certainly no conservative in the British or American sense. Coming from humble origins—his father started out as a scrap-metal merchant—he poses as the champion of the "little guy" and the *Mittelstand*, Germany's small and medium-sized companies, railing against corporate fat-cats and American-style "hire-and-fire" practices. His central values, he says, are social justice, individual freedom and tolerance.

In Bavaria, Germany's biggest and second-most populous state, which he has governed since 1993, he has shown himself to be more of an interventionist than a free-marketeer, pumping €4 billion (\$3.99 billion) of privatisation proceeds into high-tech industry. Bavaria now prides itself on being one of the most technically advanced regions in the world. The net number of companies setting up there each year is the highest among Germany's 16 *Länder* (states). It leads the country in the number of patents taken out each year. Bavaria, once one of Germany's poorest *Länder*, is now one of the richest.

But how much of this is Mr Stoiber's do-

ing? When he became premier, he took over a state that was already flourishing. Long predominantly agricultural, Bavaria has had the advantage of being able to build its industry from scratch. Many of its best-known companies, like Siemens and Allianz, came after the war from Berlin and other bombed-out areas to settle in the relatively untouched southern state, acting as a magnet for others. Judicious public investment in infrastructure and generous subsidies have helped lure many more.

The state's unchanging politics has also been an attraction. Apart from a brief Social Democratic interlude in the 1950s, the Christian Social Union has ruled Bavaria continuously since the war. Franz Josef Strauss, Bavaria's premier from 1978 to 1988, led the move into technology. Mr Stoiber simply continued what his predecessor and mentor had begun. He has proved an energetic and efficient administrator, but no great innovator.

Over the nine years of Mr Stoiber's premiership, Bavaria's economy has grown by 18%—not spectacular, though well above the meagre 13% managed by western Germany as a whole. But the downturn in the world economy is now taking its toll on Bavaria too. Last year, its economy expanded by just 0.9%, ranking it a poor sixth for growth among the German states. Bankruptcies soared by 38%, giving Bavaria the highest bankruptcy rate in the land. Unemployment, while still low at 5.9%, compared with a west German average of 7.9%, has leapt by 20% over the past year. The recent collapse of Fairchild Dornier, an aerospace manufacturer, and the Kirch media empire (into which the state had sunk €2 billion) has further damaged the Bavarian leader's standing.

Mr Stoiber accuses Mr Schröder and his Social Democrats of turning Germany into

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► an economic basket case. But when Mr Schröder took over from Helmut Kohl in 1998, public spending, taxes, welfare contributions and the public debt were all at record levels. Mr Schröder has managed to bring them down a notch or two. Germany's ossified labour market, pension, tax and health systems, left virtually untouched under Mr Kohl, were all crying out for reform. Although often criticised for not having pushed through enough reform, in these respects at least, Mr Schröder has achieved more in his four years than Mr Kohl managed in his 16. If elected, Mr Stoiber might well be prepared to do more than he is at present willing to reveal. But there is nothing in his record to suggest that he would be any more of a radical reformer than Mr Schröder. Faced with fiercer opposition from the unions, he might even prove more timid. ■

Switzerland and the world

The UN will do for now

ST GALLEN

The Swiss join the United Nations next week—still very much in two minds

“WE MUST preserve our special identity,” says an influential columnist. “We must become normal,” counters a leading politician. Many Swiss somehow want to fuse both these views—and keep their country ultra-independent and ultra-democratic, while nonetheless “opening up” to the world. With the decision to join the United Nations on September 10th, you might think the normalisers were winning. Indeed, after that, the European Union too? Do not bet on it.

Most Swiss are still wary of international clubs. After a referendum in 1992,



Switzerland's democracy

Get those hands up, then!

APPENZELL

Local elections, Swiss style

“SOME intellectuals,” says the local newspaper editor edgily, “are starting to discuss whether we should continue with it.” But he was reluctant to name a single local who might actually speak out against the Inner Appenzellers' ancient custom of electing their half-canton's government by an open show of hands on the last Sunday morning of every April. They would, he explained, be damned as “traitors” by the majority who ardently feel that such traditions are vital for preserving their identity and fiercely democratic independence. Unless outside busybodies manage to invoke voting secrecy as a human right, as has happened in at least one other of the more conservative Alpine cantons nearby, the open vote, when 2,000 or so locals (in a population of 15,000 plus) fill the village square, seems likely to stay.

Only in 1971 were Appenzell men forced to let women vote in federal elections (after a national referendum). And only 12 years ago, again by a federal ruling, did women get the vote in cantonal and municipal contests.

Robert Nef, a zealous libertarian of Appenzell ancestry, argues for maxi-

mum independence not only of cantons but also of the communes within them, whose tax regimes can vary sharply. “We are going in the wrong direction,” he fears. He does not like the redistribution of tax revenues among the cantons, or other proposals for harmonising various policies of cantonal governments. Like other cantons, Appenzell tries to lure rich pensioners. It has abolished most death duties; other taxes are low.

A front-page headline last week in the *Appenzeller Volksfreund* extolled local bakers for promising to use local butter in their bread, even though that makes it expensive. Local farmers have shrunk from a quarter of the community to 4% in 20 years. For that, outsiders are blamed, as they are for most of modernity's ills. Appenzellers are fiercely opposed to Switzerland's joining any international body, let alone the European Union, for fear of being bossed about by outsiders—a term that includes people from Zurich (the commercial capital) and Bern (the political one). Last week Mr Nef was reassured to discover that few Appenzellers even knew the Swiss president's name.

they declined to join the European Economic Area. Then, in March 2001, they refused even to start talks to join the European Union. And though they voted in March 2002 to join the UN by 54% to 46%, the constitutionally necessary approval from the cantons was a much closer call. Few Swiss pundits foresee another referendum on the EU for a decade.

In the past year, however, the Swiss have cut special deals with the EU under which they get many of the economic benefits of membership. The country may, some say, emerge as a pseudo-member, able to choose its preferences *à la carte*. But political involvement and membership dues? No thanks.

Still, Switzerland's proud self-confidence—smugness, some would say—has taken a series of knocks recently. Revelations that banking secrecy had been used to deny to the descendants of Holocaust victims (and even some survivors) assets long dormant in Swiss banks made the Swiss look mean. They also made many Swiss feel prickly and victimised.

The pressure to erode Switzerland's bank-secrecy laws has increased relentlessly. The EU wants the Swiss to let it seek out tax-evaders (who are committing no criminal offence under Swiss law). The at-

tacks of September 11th have added to the pressure. The biggest Swiss banks (UBS and Credit Suisse), the powerful private banks and all four of the country's main political parties fiercely insist that secrecy is a moral principle that cannot be discarded. But the tide of international sentiment is flowing the other way.

A huge knock to national self-esteem came last year with the collapse of Swissair, the airline that the Swiss considered a monument to their efficiency and modernity. Other setbacks have also hurt. The image of Switzerland's diplomatic service as staid but at least spotless has been tarnished recently. First, the ambassador to Berlin was recalled after a Swiss tabloid accused him, unfairly as it turned out, of sexual gallivanting. Worse, another Swiss ambassador, to Luxembourg, was sacked after being put under criminal investigation on suspicion of money-laundering.

Switzerland's highly decentralised system of direct democracy, coupled with its deep affection for consensual decision-making, does not make for strong government. No wonder the populist Christoph Blocher, the leading light of the Swiss People's Party, makes people nervous. His party is both the most maverick and, at present, the most popular of the four par- ►►

ties in power. Though his own inclinations are generally libertarian and free-market, he sometimes panders to the xenophobia of many of his voters. He wants to keep Switzerland out of all those worthy bodies, including the UN (too late to stop) and the EU (still to be fended off). And his personal fortune, put at over SFr2 billion (\$1.4 billion), gives him a certain freedom to fight for his beliefs.

An opportunity to judge whether the Swiss are in benign or truculent mood will come on September 22nd, when they will be asked to endorse a plan that would involve putting the proceeds from no-longer-needed gold reserves into three boxes: one for a national pension fund, one to boost the cantons, one, inspired by memories of the Holocaust, into a fund for humanitarian causes. Mr Blocher is against that. He would put the lot into the ailing pension fund. He gives voice to the feelings of many Swiss that they have been "black-mailed" long enough into making amends for their war-time behaviour, when they were surrounded by Nazis or their allies. He also sees a quick fix to an expensive problem. If he wins, it will be a sign that the old, frugal, inward-looking, self-reliant Switzerland, UN member though it will then be, may carry on for a while yet. ■

French politics

The Bermuda triangle

PARIS

Tough times ahead for the government

BACK to work and back to reality: "The Raffarin government is the prisoner of a Bermuda triangle: an international economy in a bad way and lower tax receipts; a European Union budgetary policy which risks a recession; and the need to finance heavy spending plans." Sour grapes from the opposition as France's politicians end their summer break? Perhaps, but Jean-Pierre Raffarin, prime minister of the new centre-right government, will find it hard to dismiss last weekend's pithy diagnosis from Jean-Pierre Chevènement, a minister in the former Socialist-led government.

Consider the evidence. World markets have tumbled and may fall further. The European Union, anxious to protect the euro, says its members must tighten their belts in order to balance their budgets by 2004. And yet Mr Raffarin, with a budget deficit of some 2.6% this year, must somehow fulfil the election promises of President Jacques Chirac, notably to cut taxes while spending more on defence, health and law-and-order. Meanwhile, unemployment, at 9% of the workforce, is edging

up, and the fear lurks that trade unions will take to the streets and humble Mr Raffarin just as they did the last conservative prime minister, Alain Juppé, in 1995.

So what is poor Mr Raffarin to do? One answer is to avoid confrontation wherever possible. When France's schools reopened this week, the education minister, Luc Ferry, assured teachers that there would be no cut in their numbers next year—though only a few days earlier his deputy had noted that, with fewer pupils, fewer teachers would now be needed.

Similarly, in carrying out a promise to soften the effects of the shorter, 35-hour working week, the social-affairs minister, François Fillon, this week sided not so much with the bosses (whom else are they going to vote for?) as with the unions: the minimum wage, now splintered into six levels thanks to the phasing-in of the 35-hour week, will reach a uniform level by July 2005, with a rise for many workers of more than 11% over the three years. Moreover, though the minister will let employers increase a worker's overtime from 130 hours a year to as many as 180, his decree is likely to be valid only for 18 months.

Another answer, of course, is to play for time. Having secured agreement with its EU partners that it needs to balance its budget in 2004 only if economic growth in the meantime is at least 3% a year (roughly double this year's likely rate), France can wait for others to press for a change in the Union's "growth and stability pact". After all, Germany's budgetary position is worse than France's, so Germany's hard-line support for the pact may change once this month's elections are out of the way.

Conceivably, there is also a third answer: to rely on the left—swept from parliamentary power in the June elections—to remain in disarray, too weak to hit the government hard. Superficially, the notion looks tempting. At an annual meeting last week, the Socialist Party looked hopelessly divided between traditionalists and reformers. Competing party heavyweights, free to indulge their ambitions now that Lionel Jospin, the defeated prime minister, has chosen an abrupt retirement, concentrated not so much on the here and now as on their rival prospects for the presidential election in five years' time.

Unhappily for Mr Raffarin, there is a counter-argument, namely that the left—and, in particular, the Communist Party and the unions—needs to demonstrate its political relevance. And what better way than by mounting street demonstrations of teachers, nurses, farmers, civil servants and so on over the coming weeks? No wonder, then, that the emollient Mr Raffarin is so anxious to avoid the confrontation that eventually led to the departure of the abrasive Mr Juppé. The trouble is that fending off confrontation is not the same as avoiding the Bermuda triangle. ■

A governor's election in Siberia

Replacing Lebed

KRASNOYARSK

The contest for control of one of Russia's richest regions



IT IS like Brobdingnag without the giants. Four times the area of France, and source of a fifth of the world's nickel and two-fifths of its platinum, Russia's entire Krasnoyarsk krai, or region, has only about as many inhabitants as Boston—and despite their land's vast natural wealth, they are as poor as church mice. "Russia in miniature," a former governor called it. A place of such proportions needs a leader to match. Alexander Lebed, the charismatic former general who ran Krasnoyarsk for four years, was a big man all right, but not much of an administrator. He died in a helicopter accident in April, and 14 people are in the race for his job. The first round of polling is scheduled for September 8th.

The favourite to win is Alexander Uss, a jurist who is the speaker of the regional assembly, having been one of Lebed's sharpest critics. He plays on the popular distrust of outsiders coming in to run the krai. Challenging him for the same voters is Pyotr Pimashkov, a local party hack, and mayor of the capital. Alexander Khlopov, in close third place, could not be more different. A clever, fresh-faced 37-year-old who arrived in the region only in 1996 as boss of the giant Norilsk Nickel mining company, he now governs the northerly province of Taimyr, which contains the company town of Norilsk.

All know that they need to put Krasnoyarsk's resources to work more effectively. Metals are mined and wood is cut, but they are usually exported for processing and manufacturing, leaving the krai bereft of local industry. Taxes from Norilsk Nickel's mines provide nearly 70% of the regional administration's income. Depressed world metal prices, plus a poor economic policy and political instability under Lebed, mean that this year's reve- ➤

nues will be far lower than projected—perhaps by as much as 40%.

There is less interest in the candidates' policies, however, than in their backers. Mr Khloponin hopes to reduce Norilsk Nickel's influence by making the *krai* less dependent on it for its budget. But few believe this, not just because of the size of the company he used to run but also because it still gives him a hefty pay-cheque. On the other hand, Mr Uss's supporters, though broader-based, include big companies such as Russian Aluminium, which owns huge smelters in the region, and Yukos, an oil enterprise. They also include Anatoly Bykov, a wheeler-dealer businessman who recently incurred a suspended prison sentence for conspiracy to murder (though he is so popular that he was elected to the local assembly even while in jail in Moscow, awaiting trial). Mr Pimashkov does not have such powerful support, but at the last minute, he was almost suspended from the race on suspicions that he had broken campaign rules.

Locals, however, seem not to worry much about such issues. "Of course they will have their own interests; the important thing is that they think about the *krai*'s interests in parallel, not in second place," says Evgenia Bukharova, dean of the state university's economics faculty. A bigger concern is how they will get on after a generally acrimonious campaign. The winner will still have to deal with the losers, who will return to their current public posts. They will have to work hard to restore harmony—or else, as in Lebed's day, political infighting could make it even more difficult for the region to find the investment it needs. ■

Landmines in Kosovo

Time bombs

Cleaning up the mess

WHEN NATO demanded, during its 1999 bombing campaign, that Yugoslavia should allow refugees to return safely to Kosovo, the western coalition did not say that NATO itself had some work to do. American, British and Dutch planes dropped more than 1,500 cluster bombs on the province in three months, leaving an estimated 20,000 unexploded bomblets on the ground. Together with the thousands of landmines laid by the Serbian army, police and paramilitaries, NATO unexploded ordnance guaranteed Kosovar refugees anything but a safe return. A huge effort has been made to clean up the area, but is Kosovo now safe?

Even when the fighting stopped, sim-

Italian football

A long dry season

MILAN

The troubles of Italian football

THIS has not been a good summer for Italian football. For the first time since the second world war interrupted play, the kick-off of the leading league, Serie A, has been postponed, to September 14th. The traditional summer transfer market for players has been weak. Yet Italians talk about *calcio* as never before. The reason? Money—and Ronaldo, a Brazilian star footballer, whom Inter Milan has just sold to Real Madrid.

A financial crisis has been simmering for some time. The top teams spend too much (to buy good players and pay their salaries) and make too little (from tickets, merchandising and television rights). Until now, appalling finances were the norm. This year, however, the football authorities asked clubs to balance their books. Fiorentina—Florence's beloved team—declared bankruptcy and is now enrolled in the fourth division under another name, Florentia. Other teams, such as Parma and Rome's Lazio, have had to sell their best players. The market has been reduced to barter: players have been exchanged, but with little money changing hands. Some of the top players have been told to prepare for salary cuts.

All teams counted, as usual, on television money. But state television said it would pay just half the €84m (\$75m) it forked out last year, and pay-TV chan-

nels were interested only in the top teams. Offered a meagre €4m each at first, eight smaller Serie A teams refused to start the season. The league asked for tax breaks. It was turned down.

Then, as the transfer season was about to close, three teams decided they could afford to spend some money on new blood. One, Juventus of Turin, did it because its books are in order. AC Milan's chairman has plenty of money and loves to win (his name is Silvio Berlusconi). The third, Inter Milan, spent €91m on new players, after pocketing €45m from selling Ronaldo.

That was the biggest news of the Italian summer. Ronaldo has twice suffered career-threatening knee injuries, and was pampered back to fitness by Inter Milan—just in time for the World Cup in Korea and Japan, which he helped his country win. On holiday in Brazil, he said he wanted to move to Madrid. This may have had less to do with greed than with the current excellence of the Spanish league and of Real Madrid in particular. Inter Milan's chairman, Massimo Moratti, was upset. Supporters were flabbergasted. Acres of newspaper were devoted to the saga. The day he left, an angry mob shouted abuse and broke his car windows. So, Italy's football fans are busy. But there is no football, yet.

ply going to school or gathering firewood for cooking was a potentially life-threatening activity in many areas: landmines and unexploded bombs caused over 340 casualties in the first six months after the fighting ended, and all in an area half the size of Wales. The response, however, was unprecedented. Governments rushed to give about \$85m to tackle the problem. The United Nations' Mine Action Service took on the task of co-ordinating the many organisations paid to carry out the clearance work. Controversially, the UN decided that its clearance of known dangerous areas was to be completed by December 2001. A new Kosovo Protection Corps, part of the local administration, would then take over from the NGOs and deal with any residual landmine threat to civilians.

In spite of this ambitious exit date, the programme to clear the mines in Kosovo has been a resounding success, says the UN. The casualty rate has been reduced to about one a month. The work was handed over to the protection corps as planned, which promises to reduce casualties still further. Important lessons, the UN argues,

have been learned about effective and efficient mine clearance.

Others are less convinced. The Halo Trust, a mine-clearance organisation, has complained that the UN ordered it to stop work on a cluster-bomb site, even though unexploded bomblets remained. The UN said the site was clear. Last month, when the BBC's "Face the Facts" programme visited Kosovo, its reporters found unexploded cluster bomblets at the site, though farming had resumed and children were at play. Meanwhile, doubts persist about the Kosovo Protection Corps. NGOs have laid off more than 800 trained Kosovar mine-clearers, but the protection corps recruited 105 new and inexperienced staff. These were mostly former fighters from the Kosovo Liberation Army, who were being demobilised. Money—surprise, surprise—is also an issue.

If the problems reported by the Halo Trust and the BBC turn out to be isolated mistakes, the protection corps should have little work to do. But if many more bomblets have been overlooked, Kosovars may have to watch their step for a long time. ■

Charlemagne Fear of America, and of being left out

Why Europe will probably give in over Iraq



EMINENT Americans visiting Europe recently often seem to find themselves in a state of bewilderment, almost as if they had stumbled into some sort of parallel universe. "We in America think of September 11th as an event that changed the world," says Bill Kristol, editor of the neo-conservative *Weekly Standard*, "but the Europeans seem to regard it as an event that changed America." Robert Kagan, author of a much-applauded article on the gulf between Europe and America, comments that "American policymakers find it hard to believe, but leading officials in Europe worry more about how the US might mishandle the problem of Iraq—by undertaking unilateral or extra-legal military action—than they worry about Iraq itself."

Both observations are broadly accurate. Together they go a long way to explaining the division that has opened up between Europe and America over the past year. Most Europeans reacted with genuine horror to the attacks on New York and Washington. But they were much less likely than Americans to think that September 11th "changed everything". In private, European leaders sometimes note, a touch condescendingly, that Europeans have had to live with terrorism for many years: Britain has had the IRA, Spain has had ETA, an Italian prime minister has been murdered by the Red Brigades, and so on. So September 11th marked a new era only because it ended a period of American innocence and apparent invulnerability, not because it introduced the world to something altogether new.

Such views risk glossing over the scale and symbolism of the attacks. In a single day al-Qaeda murdered more than three times as many people as ETA has killed in over 40 years. But the European sense that September 11th was significant above all because of its effect on America leads directly to the second point, picked up by Mr Kagan. This is the fact that many European policymakers worry more about America's reaction to terrorism than about Iraq. George Bush's "axis of evil" speech animated a fear that America might launch one regime-changing war after another, setting fire to the Middle East and ripping up international law in the process. The moralistic tone of the speech also made some Europeans squirm. With the exception of Tony Blair, who shares Mr Bush's taste for epic struggles between good and evil, few European leaders are yet inclined to see Saddam Hussein quite as the Bush administration does. An

evil man? Undoubtedly. A "clear and present danger"? The Europeans still need convincing. Recognising this, Mr Blair has promised to produce a dossier of evidence about Iraq, and the Bush administration is likely to follow suit in the next month.

Might this yet bridge the divisions? Something close to a common EU position is in fact emerging. Europe would press for the readmission of weapons inspectors, urge America to work through the United Nations, and in the last resort back a war only if it had been authorised by a new UN resolution. The emergence of mainstream voices in America urging a similar course of action has given encouragement to European officials, who a few weeks ago were more or less resigned to America going it alone. An opinion poll released this week by the Chicago Council on Foreign Relations also points to a convergence of European and American views. Big majorities on both sides of the Atlantic approve of the idea that America "should only invade Iraq with UN approval and support of allies."

But things may not be that simple. What if the UN route threatens to be a dead end? It is easy to foresee how the Iraqis might spin out negotiations over weapons inspectors, or Russia or China or even France might refuse to approve a UN Security Council resolution authorising the use of force. The temptation for the Americans to choose unilateral action in preference to multilateral inaction is strong. Any prevarication, and the meeting of minds between the Europeans and Americans would probably end. Indeed dig a little deeper into the opinion polls and the divisions of opinion are still there. The Council on Foreign Relations poll found 75% of Americans favouring "use of US troops to overthrow Saddam Hussein's government". The same question appears not to have been asked in Europe. But a recent ICM poll in Britain—usually the most hawkish and pro-American country in Europe—found only 33% approval for "a military attack on Iraq to remove Saddam Hussein".

Oh, well. If you must

So what happens if the Americans ignore the wise counsels of the Europeans and the strictures of the UN? There is a common view in Washington that the Europeans whine a lot, but ultimately will always come around when presented with a *fait accompli*. Like many stereotypes, this one has more than a grain of truth to it. Even if America attacks Iraq without UN support, the Europeans may indeed still rally round. The British will almost certainly be there. Jose Maria Aznar of Spain and Silvio Berlusconi of Italy are both right-wingers and instinctively pro-American. The German government under Gerhard Schröder has been outspoken in expressing its reservations about the use of force in Iraq, but Germany is in the midst of an election campaign and might change its tune under a new government. Even the French, speculates one EU official, may ultimately "not be able to resist fighting alongside the world's only superpower."

A swift victory would also help. Many of the fears about a "new Vietnam", global instability, civilian casualties and excessive American reliance on force were expressed before the first Gulf war, before the Kosovo fighting and before the attack on Afghanistan, only to dissolve once things worked out. Another display of overwhelming American force, plus revelations about the full horrors of Saddam's regime, might quickly consign European reservations about a war on Iraq to the memory hole.

And if things go wrong? Well, there is always the satisfaction of saying, "I told you so." ■

It may also say something depressing about the future of America's telecoms industry, in which more than 50 publicly owned firms (including WorldCom and Global Crossing) are now in Chapter 11. "Some of these companies will emerge from bankruptcy," says Ivan Seidenberg, chief executive of Verizon, a big American telephone company. "They will fail again. They should be liquidated."

Another line of attack, favoured by Mr LoPucki, blames the bankruptcy courts, especially the one in Delaware, whose restructured firms refile for bankruptcy more often than those in other jurisdictions. Before 1990, Delaware had handled just one big bankruptcy case, in 1983. By 1996, it had an 87% share of the national market. Mr LoPucki says that Delaware's judges have attracted new filings by pioneering a laissez-faire attitude to their cases: creditors and debtors are left to sort things out among themselves, despite the judge's duty, under the 1978 bankruptcy act, to confirm that restructuring plans are likely to succeed. The Delaware approach has serious drawbacks: everybody fights for his share, and nobody looks after the interests of the estate as a whole. The good news, says Mr LoPucki, is that recent evidence shows bust Delaware firms are refiling less often, perhaps as the court responds to criticism. The bad news is that refilings are rising elsewhere, especially in New York, as other courts copy Delaware.

The common thread to these problems is management. As the SEC's website candidly points out, the reason why public companies almost always choose Chapter 11 restructuring over Chapter Seven liquidation is that, in Chapter 11, incumbent management keeps a grip on the company. Which is not to say that the old managers never resign. They often do: but more usually at the end of the bankruptcy process than at the beginning. Even if they do go at the beginning, they usually get to appoint new management, which is, in this sense, beholden to the old lot.

Old (or the new, less-than-independent) managers cannot be the right people to make arms' length decisions about how to restructure their companies, or to whom to sell assets, and at what price. Incumbent managers have their own battles to fight, such as preserving their pensions, rewarding their friends and, most pressing recently, staying out of jail. The bankruptcy of Global Crossing is in the hands of John Legere, who ran the firm before it failed. More extraordinary still are events at WorldCom, whose current boss, John Sidgmore, helped to cheerlead the company alongside its former chief executive, Bernie Ebbers, through the late 1990s. With their company in tatters around them, some board members are now waking up to just how bad this smells. The disgrace is that it has taken them so long. ■

Bertelsmann

Logging off

FRANKFURT

A lot has happened since Thomas Middelhoff left Bertelsmann in July

REINHARD MOHN, who built Bertelsmann from post-war dust into a global media giant, once decreed that his executives should retire at 60. Thus Gunter Thielen had been due to quit the German company's management board last month. The Mohn family, though, is still very much in charge (through both a foundation and its direct stake), and rules can be bent if need be. In late July, when Thomas Middelhoff, then chief executive, disagreed with the Mohns about strategy, he

departed. Mr Thielen took over, and instead of tending his garden he has been travelling from one Bertelsmann office to the next, telling employees how things will be on his watch.

They will be different. Mr Middelhoff's four-year tenure was marked by big deals—some brilliant successes, some failures—that doubled Bertelsmann's annual turnover to around €20 billion (\$19.8 billion). Those times are over, at least for now. Unveiling results for the first half of 2002 this ▶▶

Music file-swapping

Napster R.I.P.

The ex-king of illegal file-swapping expires, but its clones are thriving

FOR once, reports of its death do not seem to be exaggerated. This week, Napster, the pioneer of illegal music downloading on the Internet, finally prepared for liquidation after a court blocked the sale of its assets to Bertelsmann. The deal, ruled the judge, was not in the best interests of Napster's creditors. Previous reports of the file-swapping service's demise have proved premature: Bertelsmann, which owns BMG, a record label, kept backing efforts to relaunch Napster as a legitimate business. But now that Bertelsmann has decided to pare its online businesses, this time looks to be for real. This week, Napster wiped clean its website and replaced it with the words "Napster was here", and a clickthrough to a tombstone marked "Ded kitty".

To the exasperation of the music industry, however, Napster's death will not end illegal file-sharing. Even as use of Napster has shrivelled from a peak in February 2001, Napster lookalikes have sprung up. In America, the number of unique users of KaZaA, a Napster clone, shot up by 1,491% in the 12 months to June, according to comScore Media Metrix, a research group. In June, the number of users in America of KaZaA, Morpheus and Audiogalaxy, all file-sharing services, reached 14.4m, more than the 13.6m using Napster at its peak.

The record industry is struggling to regain control. It has stepped up efforts to use the courts to shut down the Napster-likes. And it has tried to wean music fans



Out but not down

off free sites by backing fee-paying operations. Yet the four main subscription services—Listen.com's Rhapsody, press-play, MusicNet and FullAudio—limit what users can do. For the most part, they rent tracks for the duration of the subscription rather than sell them; and they forbid, or limit, the "burning" of songs on to CDs. So far, only an estimated 100,000 people have signed up to such services.

Nobody doubts that the music business is in trouble. Last year, global sales of CDs were down by 5% from 2000, the first fall since the format was launched. Yet this also reflects a shift in the way people spend their entertainment dollars. DVDs have been enjoying the novelty boom that CDs did in the 1990s. The recent surge in sales of films on DVD, along with those of video-games, may be as much behind the record industry's woes as the Napster clones.

Chief executives

The curse of charisma

Superstardom is good for bosses but bad for companies

LOOK round the new faces in the boardroom these days: few have been selected for glamour. They are folks such as Glenn Tilton, brought in this week from ChevronTexaco to rescue United Airlines and described as "extremely hard-working"; Edward Breen, a safe pair of hands from Motorola who is trying to unscramble the mess left by Dennis Kozlowski at Tyco; or Sir Nick Scheele, chief operating officer at Ford and a solid contrast to the excessively colourful Jacques Nasser. Safe is in, charisma is out.

About time too. A flurry of research casts doubt on the value of charismatic leadership. In the latest issue of the *Harvard Business Review*, Rakesh Khurana of Harvard Business School argues that firms appoint charismatic bosses because they tend to believe—despite a notable lack of conclusive evidence—that a chief executive can have an almost mystical impact on a company's performance. In fact, he says, most studies suggest that 10-20% of performance depends on the economic climate and 30-45% on the state of the industry. (That still leaves 35-60%, however.)

Belief in the clout of bosses also encourages companies to dump them when things go badly. So tenure at the top grows ever briefer. And when the boss goes, companies frequently hire a charismatic outsider to save them, often somebody from a high-profile stable such as Citigroup (James Dimon at Bank One) or General Electric (John Trani at Stanley Works).

Dismissal now accounts for 37% of all departures of chief executives. Firms that sack the boss are roughly three



times as likely as others to hire an outsider as a replacement. However, argues Margarethe Wiersema of the University of California at Irvine, in a paper presented at last month's annual meeting of the Academy of Management, replacement chief executives are no better than their predecessors at improving performance. The newcomer makes little difference to either profits or the share price.

Only in one respect does charisma demonstrably pay. Another Academy of Management paper, by Henry Tosi of the University of Florida, assessed the charisma of the chief executives of 59 large American firms, and duly found no connection with corporate performance. It did, however, find that charismatic bosses receive higher total pay than their humbler peers, after discounting both company size and performance. Charisma, it seems, is as good for the boss as it is bad for shareholders.

getting better at turning the spotlight on misdeeds: a slew of scandals involving bribery, food safety and other transgressions have been paraded before the public so far this year. On September 4th, Mitsui, Japan's largest trading house, joined the roll of shame: it announced the resignations of four top executives, including its president, over allegations that the company had paid bribes to win foreign power contracts.

This counts as progress, but Japan's system still does a terrible job of spotting and eradicating problems in the early stages. That Hiroshi Araki, TEPCO's chairman, heads the committee on corporate behaviour at Japan's biggest business federation neatly illustrates this shortcoming. Having

failed as the firm's chairman, his only contribution to better governance is to resign along with its other top executives.

It seems unlikely that either businesses or regulators will learn the right lessons from TEPCO's troubles. Both its new management and the government may try a little harder to soothe public anxieties, since its plants are involved in the government's plans to introduce a controversial new form of nuclear fuel. But as energy users have less choice than consumers of beef or dairy products, both the subject of recent scandals, the pressure to reassure the public through meaningful reforms may prove weaker than it has for food producers. Alas, the fallout from this week's scandal may not scatter far enough. ■

An Asian high-frills airline

Rolling out the red carpet

SUKHOTHAI

Bangkok Airways finds profit in pampering passengers

IN SOUTH-EAST ASIA, as in other parts of the world, low-cost airlines are snatching business away from established carriers. But the region's most successful small airline is just the opposite: the high-frills, high-price Bangkok Airways. Despite charging more on the routes where it flies head-to-head with Thai Airways, Thailand's national carrier, its passenger numbers almost quadrupled in the eight years to 2001. Profits are rising too: \$2.7m last year, one-third higher than in 2000.

The trick is to treat passengers royally. The departure lounge at Sukhothai, a small temple town that is one of Bangkok Airways' hubs, is an ornate open-air pavilion. Travellers can help themselves to drinks and snacks, read magazines, surf the web, visit a ceramics museum or simply gaze out at the topiary and lily-ponds that adorn the immaculate gardens—all free of charge. This extravagance, explains Prasert Prasarttong-Osoth, the airline's founder and chief executive, is designed to please foreign tourists, who make up over 90% of Bangkok Airways' customers. Locals are not a promising market, yet: income in most Asian countries is not high enough to sustain the sort of mass traffic that low-cost airlines cater to in Europe and America. That makes foreign tourists the region's big spenders.

Most Asian airlines design their route-maps around bulk traffic between big cities. Bangkok Airways, by contrast, uses small planes to take tourists exactly where they want to go. It has devised a circular route, for example, to usher sightseers through four big attractions in Thailand, Laos, Vietnam and Cambodia, without stopping in a single capital city. In tourist destinations where there were no airports, such as Sukhothai or Ko Samui, a Thai beach resort, the airline has built one itself.

Bangkok Airways' strategy is not without risks. Its exotic route-map puts it at the mercy of several capricious regimes. For some time now, for example, the launch of routes to Mandalay and Pagan in military-ruled Myanmar has been inexplicably delayed. And applying its business model to more distant destinations might prove difficult. Tourists seem happy to splash out on short hops, but they may balk at the five-hour flight to Xian, in China—the airline's newest route. Still, in Asia's relatively small travel market, Bangkok Airways' model looks a better bet than piling them high and shipping them cheap. ■

Black empowerment in South Africa

Shades of grey

JOHANNESBURG

The government wants big industries, such as mining and finance, to do more to foster black ownership of capital

THE South African government, proud host of this week's Johannesburg summit, was somewhat embarrassed when Robert Mugabe used the occasion to justify his ruthless expropriation of white-owned farms in Zimbabwe. Yet Mr Mugabe's rhetoric has a resonance at home: for the government has long wanted the country's black majority to have a far greater share of capital and top jobs, especially in such high-profile industries as mining and banking. The phrase it favours for this policy is "empowerment".

Until now, the government has been cautious about using its clout to push change too fast. Although more local companies have explicit empowerment policies than have anti-AIDS policies, the share of capital held by black South Africans remains pitifully small. According to BusinessMap, a think-tank, the black-controlled share of the equity quoted on the Johannesburg Stock Exchange has actually dropped to barely 2%, thanks to poor performance and delistings. Although the picture among small businesses is more encouraging, the government is worried that big industries are not changing enough.

It now seems ready to force the pace. Since August, officials from the minerals ministry have been quietly negotiating with Anglo American, De Beers and other big mining companies, over details of a voluntary mining charter that would set out a timetable for moving some ownership into black hands. The trade and industry minister, Alec Erwin, says a new policy could be unveiled before October. As these talks were under way, Anglo American cannily announced on August 30th that it had sold all but 10% of its coal assets in KwaZulu-Natal province to a black-controlled company, Leeuw Mining.

The government favours a mining charter with specific targets for black ownership, to be met by an agreed date, probably a decade after signing. It has learnt from the first effort to draw up a charter. On September 6th, representatives from the country's liquid-fuels industry will report to parliament on progress made since an empowerment charter was signed by a dozen companies and the government in November 2000. It was agreed that, within ten years, non-whites should own a quarter of "all facets" of the industry.

This is proving relatively easy to achieve, at least in downstream sales of petrol, where small retailers have long

been encouraged and are often black-owned. Larger fuel companies, such as Sasol, which controls 41% of the country's oil production, have created black-owned retailing offshoots, such as Exel, and have outsourced transport to companies dominated by blacks.

The fuel industry has become a model for others to study. That explains why the mining houses, investors and currency traders were disturbed by a draft government paper circulated in August that suggested a target of 51% for black ownership in the mining industry. It was quickly withdrawn, but mining shares and the rand fared poorly for several weeks.

The government wants owners to be compensated for any capital transferred, but it has failed to make clear who would pay for half of South Africa's mining industry, which is worth nearly \$60 billion. That suggests a lack of preparation—or a government that might be happy to see white-run companies emasculated, rather than have new black enterprises created alongside the giants. Any hint that capital might be expropriated is fiercely opposed by the industry.

Even investors who have come to accept moderate black empowerment as a fact of life see the process as a tax on business. It can be managed, they say, as long as it is limited and predictable. The government must be wary of damaging the companies it is trying to transform, argues Gra-

ham Mackay, boss of SABMiller, a brewing giant. "Some governments assume that big business will always be there, whatever is thrown at it," he says. "But business can be a fragile flower."

Business leaders welcomed parts of the broader approach to empowerment set out by Cyril Ramaphosa, a black tycoon (and former union leader) whose commission on the subject reported to the government last year. It recommended some state encouragement to speed change in big business and suggested that a "one-quarter" ownership rule was reasonable for most industries. It proposed some other targets: within a decade, 30% of productive land should be in black hands; at least 40% of directors of listed firms should be black; and at least 50% of the loans on the books of national development-finance institutions should be to black-owned companies. But the commission also emphasised that economic growth is needed to smooth transition, and that business and government should agree on new measures.

Mr Erwin says that companies and the government agree that a legal approach to force business to shift capital is best avoided, and that different types of business need different sorts of persuasion. While mining remains white-dominated and prefers to offload peripheral businesses than to see change at its core, consumer-oriented companies, such as retailers and brewers, have long had a lot of black managers in senior positions. The big problem so far, says BusinessMap's Reg Rumney, has been that blacks tried to form conglomerates, just when conglomerates went out of favour.

The main barrier to further black empowerment is the question of who ultimately pays for change. Getting even a small share of the 1.5 trillion rand (\$148 billion) Johannesburg stockmarket into black hands would take a lot of money. Past efforts to create special loans for entrepreneurs who want to buy businesses have fared badly, and commercial banks are not keen to be involved. Government procurement rules favour black-controlled firms in media, transport and retailing, but annual state spending—of some 100 billion rand—cannot all be diverted to black firms. Privatisation is another avenue being explored: the second national telecoms operator must have a black-owned partner that controls 19% of the new operation. But such rules tend to put off foreign investors—and the government is being slow to privatise anyway.

The government wants change to come soon, and it will keep looking for new ways to help black South Africans. Expect its charters for the mining and other industries in the next few months to reflect both that sense of urgency in hitting targets, and also a good deal of frustration about just how to go about it. ■



A rarity down south

Face value Globalisation's new cheerleader

Can the World Trade Organisation's new boss lead the world towards freer trade?



LISTEN to the anti-globalisation protesters and you might conclude that Supachai Panitchpakdi, who succeeded Mike Moore at the helm of the World Trade Organisation (WTO) this week, has just become an extremely powerful man. After all, according to its critics, the WTO is an unbridled, secretive outfit that skews trade rules for the benefit of big business.

Unfortunately for Mr Supachai, reality is more mundane. The WTO is a fractious club of 144 member countries that acts by consensus. Any single country, however small, can block proceedings. The WTO's top man has one of the lowest salaries among international bureaucrats. And, compared with, say, the boss of the International Monetary Fund, he also has remarkably little power. He cannot even formally set the WTO's agenda. The job of heading the organisation is more like managing a bickering professional association than running a global government.

That said, the expectations of the job are high—for the WTO's boss is the single most visible advocate for freer trade. His is the best pulpit from which to goad rich and poor countries alike into tearing down trade barriers. Less visible, but equally important, the WTO's boss has a pivotal behind-the-scenes role in ensuring that global trade negotiations succeed. Though he cannot force any compromise, a politically astute WTO director-general is in a strong position to squeeze deals out of recalcitrant negotiators.

For Mr Supachai, the task is to prod countries into concluding the global round of trade talks launched at Doha last November by the deadline of December 2004. Although trade talks notoriously drag on beyond their deadlines, Mr Supachai has an extra incentive to keep to time. His own term in office is a mere three years. That is because the WTO's members, unable to agree on a new boss in 1999, split the job between Mr Moore and Mr Supachai.

Finishing the Doha agenda in a little over two years will not be easy. Not only are the negotiations broad, ranging from freeing up trade in services to exploring international rules on competition policy, but they also include some extremely thorny issues—in particular, trade protection in agriculture. Revising global trade rules, including America's favourite weapon of anti-dumping duties, is also on the table. The WTO's members have promised to focus the Doha round on poor countries, many of which felt short-changed by the previous Uruguay round.

Although rich countries know the Doha round will succeed only if poor countries see enough benefits, particularly in agriculture and textiles, the real haggling and the big political compromises on which a successful round depends still lie ahead. America's decisions to impose steel tariffs and pass a subsidy-enhancing farm bill have hardly helped the round's chances of success. At the same time, too many poor countries remain unwilling to reduce their own trade barriers, which are often far higher than those in rich countries.

The poor world's man

Can Mr Supachai help to broker a Doha deal? His biggest advantage is also his biggest handicap: he comes from the developing world. As a former deputy prime minister of Thailand, he is the first poor-country national to head a global economic institution. While waiting to take over at the WTO, he has not shied away from outspoken comments about the need to shift more of the benefits of trade to the poor world. Many poor countries see Mr Supachai as their man, giving him a powerful position from which to proselytise about the benefits of signing up to Doha in third-world capitals.

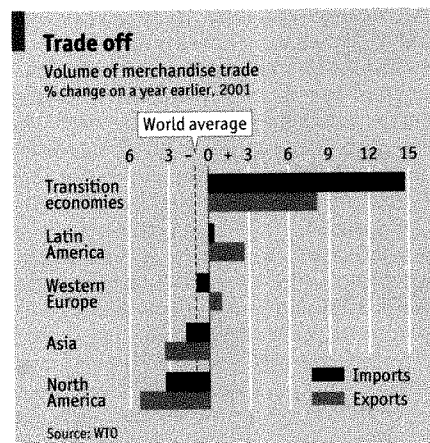
Unfortunately, goodwill in poor countries is matched by suspicion in the rich world. Mr Supachai's public comments before taking office have led Europeans and Americans to fret that he will take sides. Europeans are worried that he cares too much about freer farm trade (which Europeans find hard to swallow) and not enough about broader issues, such as rules on competition and investment, that are dear to European hearts.

Rich countries also worry that Mr Supachai sees the WTO too narrowly as a place to assist poor countries, and forgets that the bulk of global trade is still be-

tween rich countries. Last week's WTO decision to allow the European Union to impose up to \$4 billion of tariffs against America as recompense for a foreign-sales tax break which the WTO has deemed an illegal subsidy is a reminder that most of the biggest WTO decisions have nothing to do with poor countries. The fear is that, if Mr Supachai is perceived mainly as an advocate of the poor, he will be ignored by the big players.

So far, the signs are that the WTO's new boss understands this diplomatic minefield. His public statements have been measured, and he has made a point of stressing his impartiality. His ideas for WTO reform seem sensible. They include improving a cumbersome decision-making process and encouraging less litigious dispute settlement. More telling, although critics question his management ability, his appointments have been deft: for instance, Stuart Harbinson, Hong Kong's man at the WTO, and perhaps the most widely respected trade negotiator at its Geneva headquarters, has been picked as a top adviser.

Even if he can quickly quell rich-country suspicions, the real test of Mr Supachai's political savvy lies ahead. How effectively can he persuade trade negotiators to reach a compromise? At the 11th hour of trade talks, this often comes down to personal chemistry. Mr Moore played the eternally affable, backslapping politician, who smoothed feathers and brokered deals in a haze of cigarette smoke. Nobody expects that approach from the bookish Mr Supachai. His style is formal, his manner reserved. All rather Asian, in fact. The doubt is whether the Supachai style will be effective. ■





Wall Street a year on

Annus horribilis

NEW YORK

Assessing the impact of the September 11th attacks

THE past year has been the worst that most people on Wall Street can remember. All the main share indices have fallen steeply; an August rally has fizzled as share prices this week slipped back again towards their late-July lows. Investment-banking deals have evaporated. Initial public offerings and mergers, the most lucrative businesses for investment banks, are these days practically unheard of. Job losses have been both large and persistent.

The attacks on September 11th account for some of these woes. The New York Federal Reserve reckons that two-thirds of the 30,000 job losses in financial services between last September and February were caused by the attacks. Yet equity markets had cracked long before, and firms had already begun laying off staff after nearly two decades of wild expansion. Besides, it is the fall of Enron—irregularities at which were first uncovered in October—that may have greater consequences for the financial world in the long run. It led, after all, to the collapse of an auditor, Andersen; to far

greater questioning of the relationship of companies and their bankers to shareholders and clients; and to regulatory scrutiny and new legislation, of which the Sarbanes-Oxley act, passed in July, is unlikely to be the last example.

Even so, the attacks on the World Trade Centre have certainly altered New York's financial landscape. About four-fifths of lower Manhattan's office space was let to financial-services firms. More than half of these have now shifted elsewhere, usually to smaller spaces. Mid-town Manhattan has been the greatest beneficiary, but according to the New York City Partnership, a business group, 19,000 of the 50,000 financial-services workers displaced by the attacks have moved out of the city altogether. Morgan Stanley, for instance, has bought Texaco's old office in White Plains and will move many employees there. Goldman Sachs is building an office tower for its equities division across the Hudson, in New Jersey. And the New York Stock Exchange has threatened to build a second

facility in the suburbs as well.

This last move prompted New York's mayor, Michael Bloomberg, to claim that it was just what the terrorists wanted. As it is, heavy security around the exchange on Wall Street has pretty much cut it off from small restaurants and businesses in lower Manhattan, which are no longer allowed to deliver. It is tempting to conclude that even if the attacks did not kill the financial markets, they have certainly killed the Wall Street that has dominated American finance since the country's birth.

And yet. What tourists who flood the area around Ground Zero now see, beyond the garish souvenirs and the walls plastered with memorials, is a place galvanised into action like never before. The site of the World Trade Centre itself has been cleaned of several million tons of debris. Surrounding towers that were badly damaged have been fixed up. In quick succession, Merrill Lynch, American Express and the Bank of New York have all moved back into glistening buildings.

Just to the north of the World Trade Centre, a former headquarters of AT&T and of New York Telephone, now called Verizon, had served as one of the world's biggest switching centres. In the attacks, the building was hit from two sides by falling girders, and then swept by fire and floods. There was talk of knocking it down. But, says Verizon's chief executive, Ivan Seidenberg, it was important for the em- ➤

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► ployees to see the building still standing. The outside was restored, and new switching equipment was installed inside. In the months after the attacks, 3,500 staff worked to repair lower Manhattan's phones—at a cost amounting to \$1.2 billion—and over 300 are still working now. More cable lies beneath Manhattan than ever before, but with more purported security.

Before September 11th only one of New York's exchanges, the New York Board of Trade (NYBOT) had a back-up trading facility. It was also the lone exchange based in the World Trade Centre, and four of its members were killed. The other 1,600 members and exchange employees made their way across the East River to an old industrial area of Queens. There, after the World Trade Centre was bombed in 1993, the exchange had leased a small room and shipped over clunky old monitors, grumbling all the while about the \$300,000 in annual upkeep.

Right after the attacks, conditions at the site were barely tolerable, with too few phones and too little space. Some 13 trading pits were cut to two, with trading in the exchange's five commodities—coffee, sugar, cotton, orange juice and cocoa—each taking brief shifts. Currency and index trading were done in a corner.

Quickly, though, conditions improved. The army flew in a giant telephone-switching system. Food stands that were once outside the NYBOT in Manhattan moved to be near their customers. Traders created novel new systems, such as a circular price-display board of 16 flat-panel computer screens, modelled on the scoreboard at Madison Square Garden. Volumes leapt. Most striking, however, was the sudden outbreak of co-operation between the NYBOT and the New York Mercantile Exchange (NYMEX), an exchange trading energy and precious metals that once shared space with it in the World Trade Centre. The NYMEX had moved in the mid-1990s to a new facility, after which petty turf battles frustrated years of talk about a joint project. Now the NYBOT is on the verge of announcing that it is to move in with NYMEX again. That could not have happened without September 11th.

The attacks, then, explain a changed financial geography in New York. They may also have quickened the receding tide from all the financial speculation of the late 1990s. The ebb has laid bare a great deal of trickery and fraud—at Enron, Andersen, WorldCom and several investment banks—but that would have happened even without the impetus of September 11th. It is down not so much to the attacks as to the whole raft of proposed changes in accounting practices, corporate governance and the handling of investment banks' conflicts of interest that the financial world will genuinely never be the same again. ■

Disaster recovery

Preparing for the next one

Financial centres brace themselves, hypothetically

EVEN as lower Manhattan was still smoking, regulators were examining how the financial industry had held up, and how it might be strengthened against the next disaster. Thanks to well-capitalised banks, and to dealers curbing their killer instincts, the threat to financial stability proved minimal. A year on, with Wall Street firms under more pressure, another disaster might not rouse the same spirit of co-operation. It is a point relegated to a footnote in proposals released by American regulators last week on how to prepare for another disruption. "Under adverse market conditions or in the event of credit concerns about institutions," it runs, "liquidity dislocations of the type experienced immediately after September 11th could be seriously compounded."

September 11th was not what banks and regulators call a credit event. The next disaster, whatever it is, could be. Huge markets, such as that for foreign exchange or American Treasury bonds, can become gridlocked if there is a fear that somebody, somewhere, is insolvent.

Financial regulators, especially in New York and London, are trying to keep up firms' enthusiasm for their plans for disaster recovery and business continuity. British regulators have set up a website for this purpose. The Financial Services Authority last month put its staff through a business-continuity exercise at a secret back-up site.

American regulators are inviting comments over the next six weeks on their suggestions. The aim is to maintain access to real-time information and communication with other market participants—that is, from one back-up site to another. Regulators themselves, and markets, should be able to suffer a major blow and be in business again in less than four hours. Firms that matter to the financial system—15-20 big banks and 5-10 securities houses—should give priority to those markets in which they are the biggest participants, resuming business within a day.

Now banks include independent communications and information-technology systems, a weak link on September 11th, in their survival plans—more evidence that finance is all about information. The Financial Stability Forum of the G10 industrial countries, based in Basel, has drawn up an emergency contact list so that the most important financial entities and their regulators can keep links through thick and thin.

Well and good. But what form will the



The survival suite

next disaster take? Even a dozen back-up sites might not be enough to sidestep a smart cyber-attack. American regulators encourage continual testing of firms' survival plans against all imaginable events. They recommend industrywide war-games. Yet battle-weariness is setting in. Devising suitable simulations, says an American regulator, involves giving up "serial weekends". Besides, he says, their value is uncertain. With financial firms everywhere cutting costs, spending on disasters that may not happen could suffer cut-backs too. ■

Fred Alger Management

From the ashes

NEW YORK

Mauled on September 11th, an investment firm bounces back

FOR the decade of the 1990s, Fred Alger Management had the best record of any fund-management firm in America. Gains on its Spectra mutual fund averaged 29% a year, 11 percentage points better than the broad-based S&P 500 index. The firm hunts for companies with the potential for unusually strong growth, and financial markets in those days were unusually receptive to the approach. In 2000 Alger's performance was hit hard, along with other so-called growth investors. Then, a year ago, the firm itself was all but destroyed. Alger's headquarters were on the 93rd floor of the World Trade Centre's north tower. All 35 people at work that morning died, including David Alger, head of the firm since 1995, when his brother ►►

► Fred retired, and most of the firm's team of stock-pickers.

Rather than close the business, however, the decision was made to rebuild around the living. One, a portfolio manager named Dan Chung, who is now Alger's chief investment officer, had been with Tyco International on the morning of September 11th; its chief executive, Dennis Kozlowski, was attempting to reassure investors about his conglomerate. Another employee was dropping off a child at school. A third was on the way to the lift when the planes hit.

Reconstruction started immediately, and hidden strengths were found. Prosperity and the technological advances of the 1990s meant that the firm had built robust systems. A back-up facility had been established 50 miles away, in central New Jersey, and when Mr Chung arrived on September 13th to see what was left of the business, every record and every research note was found meticulously preserved. Fred Alger came out of retirement, and when the markets reopened on September 17th, he and Mr Chung were large buyers of shares in Wall Street brokerages, whose valuations were plunging. Profits from those investments improved the performance of an otherwise poor year.

Next came the recruiting of new staff. People on Wall Street pride themselves on not being sentimental, yet Alger had deep ties. Unlike most investment firms, it had never used the research of Wall Street banks. Instead, it typically hired university graduates with a background in areas unrelated to finance, and then put them through a gruelling training in research. Over the years many left to hold top jobs at other asset-management companies. After September 11th calls went out, and alumni came back from Prudential Securities, Seligman, Oppenheimer and others. By January the investment-management staff were up to 25, one more than before. A new headquarters was made out of the well-appointed (second-floor) space left by a failed dotcom, on lower Fifth Avenue.

Outside Alger's control were the markets themselves. The firm's distaste for Wall Street's share touts meant that it had avoided investing in Enron and WorldCom. Even so, it has not been spared. Assets under management have shrunk by 23%, to \$10 billion, mainly because of the stockmarket's fall, but also because some clients pulled their money out.

Alger is optimistic as usual. It reasons that, on any long-term view, America will continue to grow. It is putting money into businesses that are increasing their market share, including casinos (Mirage), cruise lines (Carnival) and even trucking (J.B. Hunt). Even in difficult times, says Mr Chung, "good companies create value". He seems to be describing his hopes for Alger as much as for its investments. ■

Terrorism insurance

Look, no umbrella

NEW YORK

Is a federal backstop for terrorist insurance necessary?

A GOLDEN rule of insurance is that you do not underwrite a risk that cannot be quantified. Last year's terrorist attacks resulted in the biggest insured losses ever, worse than any scenario in the risk models that insurers use to determine possible maximum losses. Warren Buffett, head of an insurance-dominated conglomerate, which bore about \$2.4 billion of the roughly \$40 billion of insured losses caused by the attacks, has told his shareholders that terrorist risk has become impossible to quantify. It cannot be insured any more, he says, unless the government acts as insurer of last resort.

Lawmakers in Washington, DC, have been at loggerheads on this issue for nearly a year. Last November the House of Representatives passed a draft bill to make the government provide loans for up to 90% of the losses caused by terrorism, for a three-year period. In June the Senate passed a more generous two-year scheme, and the two chambers were still battling when they went off on summer holiday. They

may yet reach a compromise between the end of their break this week and September 11th. But American insurers, lobbying for a federal backstop, are not betting on it.

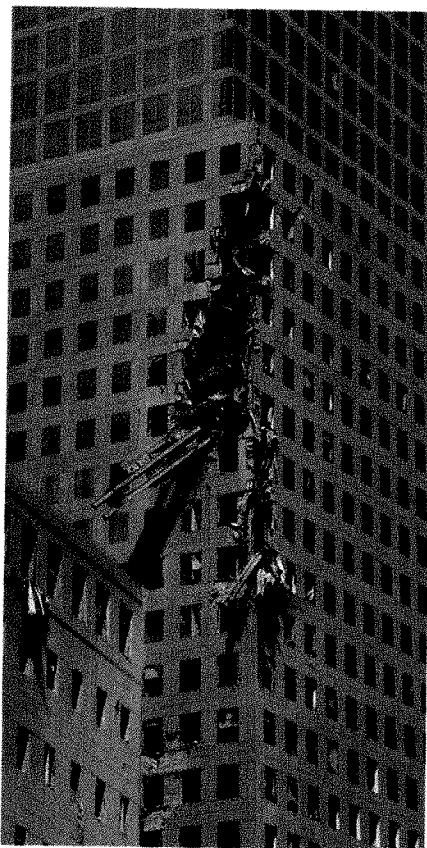
Before the terrorist attacks last September, insurance of terrorist risk was just part of general property and casualty policies, for no extra charge. Now insurers are excluding terrorist risk from their property and casualty cover, and reinsurers are refusing to insure primary insurers against terrorism. Such exclusions are allowed in all states except New York, California, Texas, Florida and Georgia, for all policies except those covering worker's compensation, and fire damage. A limited market for terrorism insurance on its own has developed in the past year—Lloyd's, AIG, Ace and others write separate policies—but such cover is expensive, and not available to all.

About half of American businesses have no terrorism insurance, a shortfall which is a threat to economic growth, according to a report by Congress's Joint Economic Committee, published in May. The property industry claims that projects worth an estimated \$8 billion have been abandoned or delayed because they could get no insurance.

Unfortunately, differences in the two houses' proposed bills remain wide. The Senate's plan calls for the government to cover 80% of losses up to \$10 billion resulting from a terrorist attack, after insurers have paid a deductible based on their market share. For losses over \$10 billion the government will cover 90%. The House plan is far less generous. It would provide loans to the industry to cover 90% of terrorism losses over \$1 billion as well as loans to individual insurers if their losses exceed \$100m and one-tenth of their premiums and surplus capital.

However, the main bone of contention between the chambers is the proposed limits on lawsuits, says Robert Hartwig at the Insurance Information Institute. The House intends to introduce measures to curb predatory lawsuits. The Senate's Democrats oppose such a curb, under pressure from the Association of Trial Lawyers, a big donor to their party.

Why all the fuss, when, according to some, the government could stay out of it altogether? Having no federal backstop did the market a lot of good, says Kenneth Froot at Harvard Business School. A new federal programme might only create more red tape. In the private sector, new methods of risk modelling are being developed, such as the Terrorism Loss Estimation Model, released this week by AIR Worldwide, an insurance advisory firm. As it is, the government has an implicit role in terrorism insurance, when the chips are down. In the event of another big outrage, it would presumably step in, as it did briefly after last year's attacks. ■



This calls for Uncle Sam

Terrorist finance

Still flush

Islamic charities, commodities and hawala are the key to al-Qaeda's money

IN SPITE of America's efforts to starve it of money, al-Qaeda probably still has plenty of cash. The war on terrorists' funds was launched with the dramatic freezing of the assets of dozens of individuals and organisations: over \$110m in all. But the initiative has faltered, according to a UN report published this week. Perhaps the blacklists gave the impression of vigorous action against terrorist financing. Yet they were only ever a small part of the task. The next and harder stage relies on the actions of countries other than America, including many in the Middle East.

Al-Qaeda was said this week to have shipped gold from Pakistan to Sudan. Investigators have already been exploring how terrorists use commodities and informal, trust-based ways to move money, known as *hawala*. They are also trying to tackle the problem of Islamic charities. The biggest are funded by Saudi Arabia's royal family. The vast majority legitimately help the Muslim poor, but some certainly finance al-Qaeda.

America has blacklisted a handful, including, jointly with Saudi Arabia, the Bosnian and Somali branches of the Saudi Arabia-based al-Haramain Islamic Foundation. The foundation recently persuaded the Bosnian government to lift the freeze on its assets, however. Meanwhile, Matthew Levitt of the Washington Institute for Near East Policy says, American officials despair that Saudi Arabia will ever admit that the domestic headquarters of any Saudi charities (as opposed to their foreign arms) might have colluded in the misuse of funds.

The kingdom has taken some preventative steps, such as ordering charities to tell the foreign ministry about new overseas projects. Ideally, says a report prepared for an upcoming meeting on charities and terrorism under the auspices of the Financial Action Task Force, the world's main anti-money-laundering body, charities should document employees, projects and possibly donors, as well as running field audits to ensure that money has not gone astray.

A lawsuit filed on behalf of the families of people who died on September 11th is less tactful. It accuses eight Islamic charities, as well as members of the house of Saud, of financing al-Qaeda. Although the American administration is unlikely to co-operate publicly with the lawsuit, says a senior official, it is taking its evidence seriously and hopes to benefit from any fresh

Initial public offerings

Spun gold

NEW YORK

Did Wall Street firms bribe bosses with shares?

IT IS fashionable nowadays to criticise the Securities and Exchange Commission (SEC) under its current chairman, Harvey Pitt, and to praise its record under his predecessor, Arthur Levitt. Yet Wall Street's latest scandal, over allocations to corporate bosses of shares in hot initial public offerings (IPOs), allegedly in exchange for investment-banking business, shows how Mr Levitt's SEC missed a big trick.

Back in 1997, reports that Robertson Stephens, a Silicon Valley investment bank, was "spinning" IPO shares to executives who rewarded them with banking mandates prompted an SEC probe into the practice. The probe was soon abandoned. The practice boomed, becoming one of the more lucrative ways in which executives combined with Wall Street to abuse ordinary shareholders.

On August 30th Citigroup told congressional investigators that in 1997-2000 it had allocated IPO shares to Bernie Ebbers that had generated profits of \$11m for the former boss of WorldCom, a telecoms firm which was a big Citi-

group client, and is now bust thanks to fraud. Other WorldCom executives had also benefited. Citi claims that these allocations were not in return for investment-banking work; rather, they were a reward to the best customers of its private-banking arm. Underwriters and issuing firms are free to allocate shares however they wish, Citi notes—while in the same breath promising to change its allocation procedures.

Citigroup has yet to show that it was as generous to other private-banking clients who could not offer potential investment-banking business in return. Its "host of benign" explanations for why some shares were allocated retrospectively, giving executives a risk-free gain, seems thin. So does its claim that Jack Grubman, until last month the bank's top telecoms analyst, played no part in allocating shares to executives. Among the documents that Citigroup sent to Congress was a memo copied to Mr Grubman that listed executives at several telecoms firms who had expressed interest in shares in IPOs.

Regulators and the courts will have to decide whether allocations of shares to executives were, in effect, bribes. If so, the punishment could be severe. Nor is Citi the only firm at risk. Credit Suisse First Boston gave shares in IPOs to executives minded to award it investment-banking business, via so-called "Friends of Frank" accounts, named after Frank Quattrone, its top technology investment banker.

CSFB and Goldman Sachs now form part of the congressional investigation. And Morgan Stanley may soon face scrutiny over the role of Mary Meeker, formerly its top Internet analyst.



leads that the families' legal team turns up.

That al-Qaeda is making more use of gold and *hawala* to move its money about is, in one sense, a sign of success: vigilance on the part of mainstream financial institutions has forced it to look for alternatives. But tracking terrorists' use of commodities—even the assets of three Yemeni honey concerns have been frozen—will take time, simply because the idea of monitoring trade for this reason is new to countries in the Middle East and elsewhere. The task-force's annual report calls on the United Arab Emirates to require gold and jewellery dealers to identify and keep records on their customers. Dubai especially is described privately by American officials as a

centre for trade-based money-laundering.

If countries refuse to take the steps that America and its allies demand, what then? When the task-force came out with its recommendations against terrorist financing last year, it threatened to name-and-shame offending countries, from this June onwards. Both America and Britain, worried about relations with other countries, have since backed away from this. As the war on terrorist money becomes more political, it will be conducted increasingly behind the scenes (there are secret lists of al-Qaeda backers, for instance, as well as public ones). It will in future become even harder to tell if the effort to cut off terrorist finances is having any effect. ■

Japan

The not-in-time economy

TOKYO

It is easy to see why the Nikkei has hit a 19-year low

ONCE again, Japan is paying the price for waiting. A combination of weak demand at home and bad economic news from America raised fresh doubts this week about whether its recent pick-up in output is here to stay. After putting off reforms, fiddling with the stockmarket and holding their breath at the end of the financial year in March, Japan's policymakers find themselves not far from where they were six months ago. Only now they are a little deeper in debt, have more countries rated above them in the international-bond tables, and have fewer ways to disguise their bad decisions.

Following signs of stagnant demand from America, investors sold off shares in exporters such as Sony, Toyota and Honda. Since a handful of such firms have supplied most of Japan's good news this year, shares in other domestic firms suffered as well, helping this week to drive the main Nikkei share index briefly below 9,000, where it last was in 1983. Because banks must report interim results at the end of this month, and must add losses on all those shares to their already weak balance sheets, confidence in the financial system is more than usually shaky.

This familiar cycle does not appear, despite a lower stockmarket, to be jangling nerves the way it did six months ago, when a weak yen and the looming repeal of insurance on some bank deposits raised the stakes. But in other respects, the situation has grown less encouraging. Earlier this year, optimists could at least take solace from signs that the economy was rebounding in the first quarter, from a dismally deflationary 2001. It now turns out, however, that all of that growth was illusory. After revising the way it tots up the

figures, the government announced at the end of August that GDP growth had been zero in the first quarter, not the 5.7% annual rate that was announced earlier.

The second quarter was better, but not especially reassuring, with GDP rising at an annual rate of 1.9%. Industrial production rose sharply in April and May, but it tailed off again in June and July. Domestic demand refuses to show a convincing bounce, leaving the economy desperately dependent on those exports and overseas earnings. Even as Honda and Toyota have racked up profits in America, for example, domestic car sales have fallen year on year for the 12th straight month.

Things may yet turn around a bit. Surveys of small firms have shown rising confidence recently. Richard Jerram, chief economist at ING Barings in Tokyo, points to recent consumer surveys, which have been a good leading indicator and which suggest that deflationary pressures may soon ease up a little as well. And there is always luck: demand from overseas may perk up again. None of this will mean much, however, if domestic demand does not strengthen, with at least a mild uptick in capital investment. Otherwise, another white-knuckle March, when the financial year comes round again, may not be too far off. ■

Unit Trust of India

To the rescue, once more

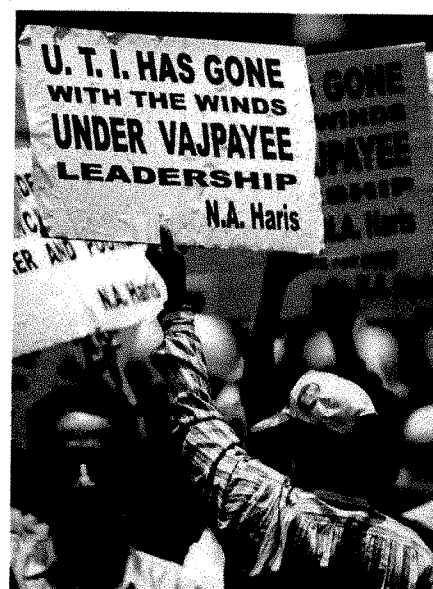
MUMBAI

And that's final

ON AUGUST 31st the Indian government announced its biggest-ever bail-out of a financial institution. The rescue of Unit Trust of India (UTI) will cost \$3 billion, equivalent to a third of its assets under management. That takes the total cost of supporting this state-owned mutual-fund manager, which is the country's biggest, to around \$4 billion. Its main fund, US-64, has been bailed out twice already in the past four years.

Of the \$3 billion rescue package, just under half will go to support US-64, with the rest going to other mutual funds managed by UTI that face a shortfall between the returns they guaranteed investors and the market value of their assets. UTI itself will be divided into two parts: a sick part, consisting of funds that are being rescued, to be nursed by the government, and a healthy one run by professional managers that might be privatised later.

The bail-out is meant to reassure 29m investors in UTI, a big political constituency, and to revive a stockmarket worried



Not the end of the story

about a distress sale of assets—UTI is the largest single investor. The cost of the bail-out will rise if the market now falls, because, under the rescue plan, the government will pay unit holders the difference between the fixed price promised to them and the market value of assets.

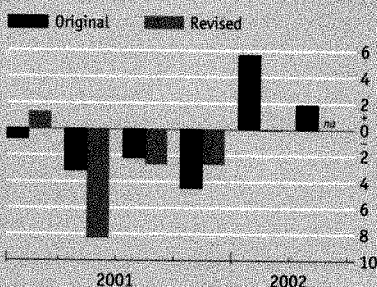
The asset manager's chairman, Meleveetil Damodaran, a finance ministry bureaucrat who took charge last year, says the government expects eventually to wind down its commitments to the old, protected UTI funds. The government hopes that an orderly exit from these funds will cost less than if there were a run on them. Orderliness might prove hard to manage. Already, more sops have been promised next year. Investors in US-64 will get tax breaks, while government-guaranteed returns will extend beyond May next year, when they were to end.

The healthier bit of UTI that is to be run by professional managers will be more than twice the size of the biggest private-sector mutual fund, Prudential ICICI. Privately managed funds, including those run by foreign companies such as Prudential, Templeton and Zurich Financial, are growing. At the end of July their combined market share stood at 47% of assets under management, just ahead of UTI, whose market share has fallen to 45%, from 65% a couple of years ago.

Perhaps private firms will one day be interested in UTI. But first the plan to privatise UTI has to be vetted by parliament, which could take forever. Given their opposition to the privatisation of state oil and telecoms companies, India's politicians might well thwart a UTI sale. Another possible buyer is Life Insurance Corporation, which is state-owned. That would be a disaster. India's new insurance regulator recently warned it over guaranteeing high rates of return on its insurance products. ■

Revising history

Japan's GDP, % change on previous quarter, at an annual rate



Source: National statistics

Economics focus To burst or not to burst?

Was Alan Greenspan really powerless to stop the stockmarket bubble?

EVERY August central bankers and economists gather in the Rocky Mountain resort of Jackson Hole, Wyoming, for the annual symposium of the Federal Reserve Bank of Kansas City. This year Alan Greenspan, chairman of the Federal Reserve Board, used the opportunity to give his fullest defence yet against charges that he should have raised interest rates in the late 1990s enough to prick the stockmarket bubble before it got too big. The Fed, like other central banks, takes account of rising asset prices (shares or property) to the extent that they boost spending and hence future inflation. Yet a financial bubble can inflate even when inflation in goods and services remains low. And when a bubble bursts, it may cause severe balance-sheet strains—of the kind now showing in America.

Mr Greenspan offers two defences for failing to respond to the bubble. First, he argues that it was impossible to be certain that the rise in share prices in the late 1990s really was a bubble until after it had burst. Second, even if a central bank can detect a bubble, it is not clear what it can do. A small rise in interest rates might not work; by increasing confidence in the central bank's powers, it might even boost share prices further. On the other hand, a sharp increase in rates could trigger a recession—the very outcome central bankers would be seeking to avoid, says Mr Greenspan.

Detecting and pricking bubbles are both difficult, but that is not a justification for doing nothing. Monetary policy always deals with uncertainty. Judging whether a rise in share prices is justified by an increase in productivity growth is surely not that different from deciding whether the potential rate of growth has increased or decreased. Central banks have to do that to estimate the gap between actual and potential output—itsself an important input for forecasting inflation. A central bank does not need to be completely certain to act. Unrealistic profit expectations built into share prices in the late 1990s pointed to the strong probability of a bubble.

Supporters of Mr Greenspan argue that central bankers are unlikely to have more information or to make better judgments about share prices than markets do. Yet central bankers have longer time horizons and different incentives from the private sector. In other words, in many circumstances they may respond differ-

ently to the same information.

What of Mr Greenspan's second claim, that a small rise in interest rates might prove counterproductive? He cites three years—1989, 1994 and 1999—when share prices continued to rise even as the Federal Reserve raised rates. All the same, the impact of higher rates might be different if the Fed were actually to state that its aim was to cool the stockmarket.

There may be no painless way to deflate bubbles. Yet the correct test is not whether a bubble can be deflated without some loss of output. Rather, it is whether the early pricking of a bubble causes less pain than letting it grow only to burst later. The longer a bubble is allowed to inflate, the more it encourages the build-up of other imbalances, such as too much borrowing and investment, which have the power to turn a mild downturn into something nastier. If the Fed had let some air out of the bubble earlier, America's economy might now be better placed for future growth.

A recent paper* by Claudio Borio and Philip Lowe at the Bank for International Settlements addresses the problem of identifying bubbles. The authors argue that the focus on asset-price bubbles alone is wrong. It is only when a boom in

share prices or house prices is combined with a big increase in debt and over-investment by firms that economic and financial stability is threatened. From a study of 34 countries since 1960, Mr Borio and Mr Lowe conclude that a simultaneous surge in both credit and asset prices gives a pretty reliable warning of financial problems ahead. The case for a rise in interest rates is therefore stronger when asset-price rises go hand-in-hand with rapid growth in credit—as in America in the late 1990s.

Fuelling the fire

Admittedly, for the Fed to justify an increase in interest rates when inflation was low would have been hard—but not impossible. It could, for instance, have argued that raising rates and so containing financial imbalances would avoid future economic instability and hence a large undershoot in future inflation.

Central bankers do not have a political mandate to respond to asset prices. Even so, Mr Greenspan could still have done more to warn investors about their irrational exuberance (which he talked of as long ago as December 1996). At least he could have refrained from talking up share prices, if unintentionally, through his enthusiasm for the new economy. Mr Greenspan repeatedly expressed confidence that America's productivity growth had risen significantly, encouraging investors to form unrealistic profit expectations. Estimates of productivity growth have since been cut. Goldman Sachs has shaved its estimate of trend productivity growth to 2%. Two years ago, most economists had their sights on 3% or more.

One positive sign: in his speech Mr Greenspan did at least accept that the Fed should try to identify bubbles and to incorporate them into economic models. But for the moment he doubts that central banks can do anything about them.

If the American economy recovers fast, then Mr Greenspan's policies will be vindicated—if bubbles left to burst of their own accord result only in a mild recession, central banks do not need to prick them. If America suffers several years of slow growth as its financial imbalances unwind, however, the verdict must be that the Fed got it wrong. ■



* "Asset prices, financial and monetary stability: exploring the nexus", by C. Borio and P. Lowe. BIS Working Paper No. 114, July 2002



Sustainable development

The bubble-and-squeak summit

JOHANNESBURG

So what was achieved by ten days of talking?

SOME Britons are fond of a dish made by mashing and heating the remnants of previous meals. The mysterious repast known as bubble-and-squeak is not haute cuisine, but it is good in parts. Much the same might be said of the United Nations' World Summit on Sustainable Development that closed this week. Almost everything on the menu at Johannesburg had been served up before, at one conference or another.

Thus, development targets were rehashed from a turn-of-the-millennium meeting in New York. "New" aid packages from rich countries proved to be warmed-up pledges first made at a finance-for-development bash held in Monterrey, Mexico, this year. On the side, talks on market access and farm subsidies reconfirmed promises on freeing trade that were made at talks in Doha, Qatar, last year. The main green "successes" were unilateral declarations of support for a protocol on greenhouse gases that was drawn up in Kyoto in 1997.

The UN man in charge of the summit, Nitin Desai, says all this was to the good. The official meeting of 21,000 delegates was not supposed to raise big new issues, but rather to consider well-known problems and find practical ways to solve them. Delegates, presidents and spin-docs queued up to say the meeting was about "actions not words", "starting a new

era of implementation" and "creating partnerships". The Rio environment summit ten years ago produced a well-received final declaration, but little of substance followed. Clare Short, Britain's development minister, says the reverse is true, on both counts, of this year's talks.

Squeak less, bubble more

Although Ms Short and other government delegates were unimpressed by the final Johannesburg text and its separate political declaration, they point to a few specific commitments and a useful emphasis on fighting poverty rather than on conservation. Most striking was a promise to cut by half the number of people with inadequate water and sanitation, and to try to do so by 2015. The evidence from unglamorous sewerage and hygiene projects is that helping an extra billion people in this way will do much to reduce diarrhoea, cholera and other water-borne diseases that strike the poor disproportionately.

The UN Development Programme (UNDP) is charged with monitoring progress towards this target and towards other, restated, Millennium Development Goals—to halve the number of people living in absolute poverty, to cut illiteracy and to cut child mortality, also by 2015. It will do so mostly by collecting new and reliable statistics and by presenting annual country-by-country reviews. With proper

Also in this section

74 Ethanol-powered cars in Brazil

75 How harmful is Ecstasy?

figures and accepted priorities for aid spending, governments should be better able to fight poverty. Money would help too: America, Britain and France each said that aid would be channelled towards poor-country sanitation projects.

Although Africa is likely to benefit from anti-poverty measures, some of its leaders did little to help themselves during the ten days of talks. The leaders of Zimbabwe and Namibia took turns haranguing western leaders, especially Britain's Tony Blair, for meddling in the continent, even though southern Africa, much of which is in the grip of famine, depends on foreign help to feed around 14m people. Levy Mwanawasa, Zambia's president, said again that his government would refuse "poison" as food aid, and will therefore turn away genetically modified (GM) grain, despite reassurances from Europe, America and the World Food Programme that there are no health risks involved. Yet the WFP has enough GM grain stocks to feed for two months the 2½m Zambians who are suffering from famine. Its non-GM stocks will last only two more weeks, and will be hard to replenish.

On environmental matters, the summitteers agreed to do more to conserve and restore fish stocks, in part by promising to guard ocean areas already designated as protected—with 2015 chosen, once again, as the date for achieving success. Leaders from China and Estonia used their five minutes in the plenary session to announce ratification of the Kyoto protocol. This sets out rules for how much rich countries should cut emissions of greenhouse gases, such as carbon dioxide, that are thought to add to global warming. The prime ministers of both Russia and Canada promised to ratify soon. When they have done so, the protocol will have ►►

► enough support to come into force, despite America's refusal to agree to it.

So much for the specifics. Much of the rest was mushy and imprecise. After resistance from oil-producing countries led by Venezuela, from America, and from poor countries worried by costs, the final text includes no targets for the use of renewable energy sources such as wind, sunlight and waves. The Americans opposed "unrealistic" targets for these technologies in particular, and any outside meddling in domestic energy policies in general.

Environmental activists and some American renewable-energy companies were predictably disappointed. But enthusiasts said they were happy that, for the first time, such a UN conference had declared an "urgent need" to "increase the share of renewables" in global energy production. European Union countries and Brazil had wanted targets, and may well announce them unilaterally. South Africa said it would reveal its target for renewable-energy production within a few weeks. Seven of the world's largest energy companies also announced that they would share technical plans on how to get more solar-powered generation plants to rural areas in poor countries.

Such private efforts were reckoned by the summit's cheerleaders to be its main success—although many activists were furious about "corporate takeover" of the meeting, calling it a victory for greed and a tragedy for the poor and for the environment. Business was barely present in Rio ten years ago, but some 700 companies and 50 chief executives attended the Johannesburg talks.

This week Mr Desai happily rattled off lists of 230 "type 2" initiatives agreed between governments, companies and non-governmental groups (type 1 initiatives are those between governments alone). Some will no doubt prove to be public-relations stunts, but the successful ones are meant to import private money and expertise into development projects. HSBC, a big bank, plans to spend \$50m over the next five years on lending 2,000 of its staff to work on projects run by environmental groups such as Earthwatch. Alcan, a Canadian aluminium company, says it will help villagers in Bangladesh to remove arsenic from their water supplies.

Mark Malloch Brown, the UNDP's boss, also wants more official aid used to "leverage" private cash into poor economies. He thinks it might be used to cut the cost of hooking villages up to local electricity-generating plants, or to subsidise the prices charged. But some firms are already taking it upon themselves to do things previously left to governments. Shell, a large oil company, plans to put solar panels in thousands of rural homes in poor countries. Various mining companies that operate in southern Africa, including Debswana, De

Beers and Anglo American, have promised free anti-AIDS drugs and health care for infected workers and their families.

These public-private partnerships may have more impact than all the fine words spewed at the Rio talks. But many delegates in Johannesburg say that this should be the last great UN gabfest on sustainable development. "The time for these general summits is gone, we don't need another meeting like this in 2012, this is enough" said Anders Rasmussen, Denmark's prime minister and the EU's current president. Smaller, focused meetings should be expected instead of jamborees that take too much effort and usually produce slight results. And yet, as eaters of bubble-and-squeak sometimes find, another plateful is often just too tempting. ■

Renewable fuels

Driven to alcohol

SAO PAULO

Brazil has another try at running its cars on ethanol made from sugar cane

ONE of the deals struck at the Johannesburg summit on sustainable development was a pact between Brazil and Germany to develop a scheme in which German companies will subsidise Brazilians to buy cars that run on ethanol instead of petrol. That should reduce emissions of carbon dioxide, the principal greenhouse gas covered by the Kyoto protocol, an agreement intended to curb global warming. The "credits" that the German firms earn from this will count towards their country's targets under the protocol. Brazil thinks it will benefit by reducing its dependence on imported oil.

The proposal is part of Brazil's drive to revive its ethanol-fuel programme, which was a huge, though brief, success in the mid-1980s. At its height, three-quarters of all new cars sold in the country ran on pure ethanol. But by the late 1990s this had

fallen close to zero (see chart), although all petrol sold in Brazil contains 26% ethanol, a mixture on which standard petrol engines can run without adaptation.

Sugar cane, like other plants, absorbs carbon dioxide from the atmosphere during photosynthesis. Burning ethanol made from sugar thus returns to the atmosphere what was recently there, rather than adding carbon that was previously underground. Unfortunately, turning sugar cane into ethanol uses more energy, and thus causes more greenhouse-gas emission, than making petrol from crude oil. Nevertheless, says Lew Fulton of the International Energy Agency, a sister body of the OECD, studies suggest that Brazil's present method of making ethanol fuel from sugar leads to net savings of about 50% in greenhouse-gas emissions per kilometre travelled, compared with running cars on petrol.

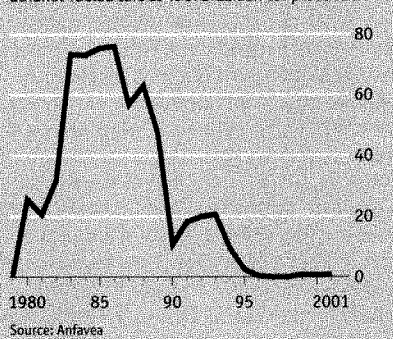
And the cuts in emissions could be much greater. At the moment, after squeezing the sugar out, the crushed cane is chucked away or burnt. Its carbon therefore returns to the atmosphere without doing anything useful. But since the cane itself is made of cellulose—in other words, polymerised sugar—it can be broken down with acid and used to make more ethanol. In America, ethanol is made from maize and other crops by turning their complex carbohydrates into sugar in this way, though this is only viable thanks to big government subsidies.

It was the high cost of imported energy after the 1970s oil shocks, rather than environmental considerations, that made Brazil switch to ethanol the first time round. As one of the world's biggest sugar producers, it assumed it would have no problem guaranteeing its motorists supplies of home-produced ethanol. But a surge in the world price of sugar meant growers could get more money from exporting the stuff than from selling it to local distilleries. As a result, many distilleries shut, leading to shortages of ethanol just as motorists were anyway tiring of the reluctance of ethanol-fuelled cars to start on cold mornings. Meanwhile, the oil shock had given way to an oil-price slump, and petrol was cheap again. Motorists therefore stopped buying ethanol-fuelled cars, and car makers all but stopped making them.

Recently, the oil price has risen, as have worries about Brazil's balance of payments and foreign debt. So the government has decided to try again. It has leant on car makers to introduce new models that run on ethanol and, this month, the sales tax on such cars was cut. Modern fuel-injection means that cold starts are no longer a problem. Motorists are duly returning: in the first seven months of this year, they bought 23,000 ethanol-fuelled cars, compared with fewer than 8,000 in the same period last year. Besides rising oil ►►

Running out of gas

Ethanol-fuelled cars as % of Brazilian car production



prices, the sharp fall in the real and improvements in the efficiency of sugar plantations and distilleries mean that ethanol-powered cars may no longer need subsidies to compete with petrol-driven ones, says Dr Fulton, though they still get them.

Of course, there is more to being environmentally friendly than cutting greenhouse gases. Sugar cane is notorious for depleting soil nutrients and thus being a voracious consumer of agro-chemicals. But this is being overcome. Plantations in Brazil are progressively being banned from burning foliage, and persuaded instead to leave it on the ground to compost, return-

ing to the soil much of the nitrogen that the growing plants have removed. On top of this, sugar cane grown for fuel production, rather than for food, can be fertilised using treated sewage, thereby providing a use for the growing quantities of human waste emerging from Brazil's cities.

Many details of the revived ethanol-fuel scheme are still to be worked out—such as how to manage and finance stocks of ethanol to guarantee continuity of supply. But overall, its chances both of saving Brazil money and of helping to avoid global warming look rather better now than they did the first time round. ■

Recreational drugs

The agony and the Ecstasy

A scientific row has broken out over the effects of Ecstasy

WHAT with angry parents, alarming headlines and crusading politicians proclaiming the dangers of MDMA—a recreational drug more commonly known as Ecstasy—it takes a brave, or foolhardy, individual to go against the grain. Jon Cole, an addiction researcher at Liverpool University, in England, denies that he is either, but his unorthodox views about the long-term effects of Ecstasy are still kicking up a storm. In this month's issue of the *Psychologist* Dr Cole and his colleagues argue that experimental evidence suggesting a link between Ecstasy use and problems such as nerve damage and brain impairment is flawed, and that using this ill-substantiated cause-and-effect to tell the "chemical generation" that they are brain-damaged when they are not creates public health problems of its own.

Over the past decade, Ecstasy has become the badge of youth subculture in Europe and America, and a weekend favourite with night-clubbers looking to boost the high of a night on the town. Perhaps as many as 3m people in Britain and more than 6m in America have tried the drug at some point, with an estimated 500,000 being regular consumers in Britain alone.

Overdoses of Ecstasy can kill, in part by causing ravers to overheat and drink too much fluid—which lowers the level of salt in their blood and throws their hearts out of kilter. Some 40 people died of Ecstasy-related causes in England and Wales last year, twice as many as in 2000. For all this, many users consider Ecstasy to be a soft and sociable drug, along the lines of cannabis or alcohol, rather than a dark and dangerous substance like heroin.

Drug researchers such as Andy Parrott, at the University of East London, beg to dif-

No brain damage here, mate

fer. They point to a range of studies showing that regular Ecstasy use can alter the levels in the brain of a molecule called serotonin. This substance carries signals between certain sorts of nerve cells. The result is an undermining of memory, sleep, appetite and (perhaps most worryingly for clubbers) sex drive. It can also lead to concentration problems, anxiety, impulsive behaviour and depression.

In America, those who advocate the use of MDMA in clinical practice have long questioned this experimental record. Now the challenge has come to Britain; indeed

one of Dr Cole's co-authors, Charles Grob, a psychiatrist at Harbor-UCLA Medical Centre in Los Angeles, is a leading exponent of using MDMA as a therapy.

The review carried out by Dr Cole finds fault with much of the evidence on the effects of MDMA. He is particularly concerned about research that shows long-term mental changes in Ecstasy users. He argues that these studies are flawed because they fail to control for other factors, such as pre-existing psychological complaints or other drug use. These, not MDMA, he suggests, may be causing the problems observed.

Furthermore, he reckons that research which questions the long-term damage of Ecstasy is being suppressed by scientists keen to accentuate the negative. Not so, according to Dr Parrott, who describes Dr Cole's views as irresponsible and accuses him of the same sin of selective publishing. He cites a ream of studies which refute Dr Cole's points in his response to the paper in the same issue of the *Psychologist*.

Other experts are not quite so dismissive. Michael Morgan, an experimental psychologist at Sussex University, admits that there are holes in the experimental record that need to be filled before the link between the drug and nasty long-term effects moves from correlation to causation.

For example, animal tests are a good way to see the effects of MDMA unsullied by the presence of other drugs. Dr Cole argues that, though animal studies routinely show brain damage from MDMA, few have demonstrated that this actually has any effect on an animal's daily life. But as Dr Morgan points out, the sorts of complex traits, such as impulsive behaviour, that MDMA is thought to produce in people are hard to examine in animal experiments.

Improvements in imaging technology, which can show how the brains of Ecstasy users change over time, could help. So could more sophisticated ways of measuring drug use, such as sampling people's hair. This lays down MDMA as it grows, and thus provides a record of exposure that is more reliable than users' own recollections. Dr Morgan hopes to put some of these new approaches into practice by embarking on a three-year study of 1,000 university students to deal with some critical unresolved questions, such as whether light users of the drug, who take it seemingly without side-effects, are actually storing up problems for the future.

As advocates of drug liberalisation have found, the deadweight of popular opinion admits of little dissent. Yet such dissent should act as a call to clarify the science involved—which even those who are convinced of MDMA's dangers should surely welcome, since they seem so confident of the outcome. Until the uncertainties are cleared up, however, you pay your money and you take your chance. ■





Islamic terrorism

Men in black

Is Osama bin Laden's al-Qaeda the advance guard of a Muslim holy war, or a scattered gang of anti-American terrorists who got lucky? Do any of us know?

THE most alarming conclusion to be drawn from two new books about al-Qaeda is how little we really know about it. Despite a year-long global hunt, it remains unclear how strong the organisation is, how far it extends and precisely how last September's plot was hatched and executed. Indeed, basic questions, such as how a multinational cell of conspirators in Hamburg joined up with a group of American-based Saudi muscle-men with "clean" backgrounds to launch attacks on New York and Washington still await answers. The failure to capture Osama bin Laden, or even to ascertain whether he is dead or alive, is a telling sign of general puzzlement. If western intelligence services know better than the rest of us, they are keeping their knowledge extremely quiet.

In the bewildering weeks after the attacks, the CIA depicted al-Qaeda as a ruthless network reaching into 50 countries. This hastily sketched portrait served the understandable purposes of rallying America to defend itself against a disciplined, well-prepared foe—if such it was, and who could then be sure?—and of deflecting the charge that American intelligence had been napping. What open, democratic country could have been expected to defend itself in advance against such a sneaky, hydra-headed opponent?

One year on, the truth appears less simple. In the rush to paint Mr bin Laden as a nightmarish amalgam of James Bond and

Al-Qaeda: The Terror Network that Threatens the World. By Jane Corbin. *Thunder's Mouth Press/Nation Books*; 296 pages; \$24.95. Published in Britain as *"The Base: In Search of al-Qaeda, the Terror Network that Shook the World"*; *Simon & Schuster*; £18.99

Inside al-Qaeda: Global Network of Terror. By Rohan Gunaratna. *Columbia University Press*; 240 pages; \$22.95. *Hurst*; £25 (hardback), £12.95 (paperback)

Joseph Stalin, western governments suggested that every radical Islamic group from Algeria to Malaysia was an arm of al-Qaeda. This, to say the least, is unproven. Although Mr bin Laden's camps in Afghanistan were broken up by American bombs, almost none of his putative allies across the world has retaliated. Hamas and other Palestinian groups have an ample supply of suicide bombers. Yet they have kept their focus on Israel, leaving al-Qaeda to rely on minor figures such as Richard Reid, the British-born would-be shoe bomber, to exact revenge for the Taliban's fall and the loss of Afghanistan.

These two books promise readers an inside view of al-Qaeda. But in the absence of talkative defectors they rely almost entirely on Mr bin Laden's public statements, and on court testimonies arising from the 1993 World Trade Centre bombing and the attacks five years later on American embassies in Kenya and Tanzania.

Also in this section

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In "Al-Qaeda: The Terror Network that Threatens the World", Jane Corbin traces the rise of Mr bin Laden's group, focusing on the September plot and its aftermath. Ms Corbin, a BBC journalist who has made several documentaries about al-Qaeda, credits the group for its skills and cunning. But the cascade of missed chances to detect the conspiracies form an equally important counterpoint to her gripping narrative. The first of these was in Germany, where Ms Corbin reports that the internal security agency responsible for Hamburg had only two officers on the Islamic watch, neither of whom spoke Arabic.

The unconnected dots were even commoner in America. An FBI agent's request to look into the suspicious number of Islamic radicals in aviation schools was ignored. Months later, senior FBI officials rebuffed pleas from agents in Minnesota to search the computer of Zacarias Mousaoui, who had ties to the hijackers. Despite al-Qaeda's vaunted professionalism, Mohammed Atta, the ringleader, twice entered the United States with an expired visa. Only last month, a German prosecutor disclosed that the German cell had sent more than 30 e-mail applications to American flight schools.

Blaming intelligence services for past oversights, however, is probably looking in the wrong place. Successful terror almost by definition catches authorities off guard. What matters is how well you identify and deal with the threat thereafter.

Rohan Gunaratna's "Inside al-Qaeda: Global Network of Terror", embraces the notion of Mr bin Laden as the godfather of an army of terror with foot soldiers in every region of the world. A research fellow at the Centre for the Study of Terrorism and Political Violence at St Andrews University in Scotland, Mr Gunaratna mixes his own interviews with a blizzard of secondary sources of uncertain reliability. He

asserts, without providing details, that Imad Mugniyah, a Shia terrorist and leading figure in Hizbullah, gave al-Qaeda the expertise it needed to carry out the bombings of the American embassies in Nairobi and Dar es Salaam. The back-up? A single interview with an unnamed American "intelligence community" official.

Neither book sheds enormous light on the vital question of what Mr bin Laden's surviving followers want. Are their goals global and ideological or regional and political? Is al-Qaeda's worldwide call to kill Americans and Jews the opening cry of an anti-western holy war? Or will it be satisfied if American troops leave Saudi Arabia and the house of Saud collapses?

Nobody seems to know. But having a head full of questions is no reason to drop your guard. In the past, al-Qaeda's attacks have come at intervals of 12-18 months, and Ms Corbin for one believes there will be more. Despite lingering uncertainties about the scale and nature of the threat, her book suggests a clear path for western governments: tighten borders and make warring intelligence agencies work together against an adversary which, if not quite ten feet tall, was skilled enough to land blows of incalculable devastation. ■

On screen

Boxing terror

After the towers came down

THE assault on New York made for horrible—and horribly irresistible—television. A year later, few film makers have been able to look away from the event itself. Among them are two notable exceptions.

"Avenging Terror", shown last week on Britain's Channel 4 and going out on PBS in America on September 8th, tells how the international anti-terror coalition was put together. In persuading so many key players, including Vladimir Putin, top Americans and Pakistan's General Pervez Musharraf, to tell their part direct to camera, Norma Percy has created a political narrative of surprising intimacy and authority.

Quite differently, a French television channel, CanalPlus, offered 11 directors, including Youssef Chahine from Egypt, Britain's Ken Loach and Alejandro Iñárritu of Mexico, the chance to explore their reaction to the attacks in an ensemble of short films for cinema. In the current climate they are unlikely to get much of an airing in the United States, but there may come a time when Americans will be more willing to listen to why their country continues to terrify and infuriate so many people.

Arab media

Island in the sun

Al-Jazeera: How the Free Arab News Network Scooped the World and Changed the Middle East. By Mohammed el-Nawawy and Adel Iskandar. Westview Press; 240 pages; \$24 and £16.99

TO ITS critics, the television channel al-Jazeera is the voice of terror, churning out propaganda for Osama bin Laden and Saddam Hussein. But to its many Arab fans, the six-year-old station is an oasis of freedom in the arid desert of the Arabic media. Love it or loathe it, the 24-hour Arabic news channel based in the tiny state of Qatar has become hard to ignore.

Mohammed el-Nawawy and Adel Iskandar are fans, as their over-heated subtitle makes plain. Citing what they admit are estimates, they put the network's audience at 35m in the Middle East and among the Arab diaspora. The reason for such success, they say, is that al-Jazeera sides with people against governments. Its live and often noisy debates have given a platform for dissent on corruption, human rights, Islam and the role of women, topics often ignored or suppressed in the Arabic media.

The network was set up in 1996 with \$140m—supposedly a five-year loan—from the Emir of Qatar, Sheikh Hamad. It now has 350 journalists and 50 correspondents working in 31 countries. Notoriety in the West came after September 11th, when al-Jazeera broadcast—and sold on to the western media—videos of Mr bin Laden's pronouncements. When American officials asked Sheikh Hamad to stop al-Jazeera from giving terrorists a voice, he politely reminded them that for years they had been nagging Arab governments to open up their media. The Bush administration's dislike of al-Jazeera has not stopped Colin Powell, Condoleezza Rice and Donald Rumsfeld from appearing on the channel.

Messrs el-Nawawy and Iskandar struggle to defend the network against its detractors. They appeal at one point to the dubious idea of "contextual objectivity": al-Jazeera presents an Arab view of the world, just as CNN presents an American one. This is at best a muddle, at worst, an evasion. As to charges of being pro-Taliban and pro-Saddam, the authors are reluctant to acknowledge that the network has indeed pulled its punches in return for exclusive footage from Kabul and Baghdad.

Al-Jazeera's true flaw, however, may lie in its relationship with Qatar. Not only has that loan not been repaid; according to the authors, the Qatari government has also been pumping as much as \$100m a year into the channel. What is in this for the

emir? Creating it was an act of sheikhly one-upmanship which gave the ambitious ruler of a postage-stamp state new leverage over his neighbours. In "Satellite Realms" (I.B. Tauris), published earlier this year, Naomi Sakr provided the broader context in which al-Jazeera's rise should be seen. The explosion of satellite television in the Middle East since CNN's victory in the Gulf war has been dramatic. But, as she makes clear, the region's governments have gone to great lengths to make media companies stick to a code of conduct, which in itself is code for not being overly critical. Powerful countries, principally Saudi Arabia, have bullied advertisers to punish those, like al-Jazeera, who disobey. Deprived of commercial autonomy and dependent on princely handouts, al-Jazeera illustrates the fragility as much as the vibrance of Arab societies. ■

Civil liberties

Easy to lose

It's a Free Country: Personal Freedom in America after September 11. Edited by Danny Goldberg, Victor Goldberg and Robert Greenwald. RDV Books; 362 pages; \$19.95 and £14.99

Terrorism and the Constitution: Sacrificing Civil Liberties in the Name of National Security. By David Cole and James X. Dempsey. New Press; 240 pages; \$16.95

IT TOOK the United States Congress six weeks after the September 11th attacks to give sweeping new powers to just about every law enforcement agency—from the FBI and CIA to the Treasury Department and Immigration and Naturalisation Service—to wiretap telephone conversations, read e-mails and monitor the Internet, as well as arrest, detain and deport suspicious individuals. The bill was more than 300 pages long, and few members of Congress had read it before they voted for in overwhelming numbers. How could anyone vote against? It was called the USA Patriot Act. Profiles in courage were few: only one senator, Russ Feingold, a liberal Democrat from Wisconsin, voted no.

Furthermore, John Ashcroft, America's attorney-general, declared that the authorities would now listen in on talks between lawyer and client if he deemed it necessary for security. And he announced for good measure that in some cases the government might use military tribunals.

To the authors of this collection, mainly civil-liberties activists, many of the legal measures introduced in the past year amount to what Michael Ratner, director ►►

► of the Centre for Constitutional Rights, describes as the "most sweeping assaults on liberties in the last 50 years". Others point out that they are anathema to American democratic values and that they cannot, in any case, guarantee everyone's safety.

These views will not be popular. But they need saying. Many times before, Americans have reacted to fears of foreigners with harsh measures only later to regret it, as Ira Glasser, a former director of the American Civil Liberties Union, notes in the opening essay.

Over the past year, the new powers were deployed most visibly against non-citizens, predominantly Muslim-Arab ones. More than 1,000 were rounded up and held for months without a lawyer, before release or deportation. Mr Ashcroft's department refuses to confirm the number, let alone the names, of those still held, though it is estimated at over 100. Arab-Americans are not an influential constituency in the United States, which may partly explain why public reaction to the restrictions of liberty has been muted.

David Cole, a civil-rights lawyer, is a professor at Georgetown University and a broadcaster on National Public Radio's "All Things Considered". His co-author, James Dempsey, was a staffer on the House Judiciary Committee. Together, and in a more focused way than in a collection of essays, they list the constitutional dangers of the war on terror. Their book will not be popular either. But civil liberties seldom are—especially with governments. ■

Other books

And do not forget...

A dozen further books to read (or avoid)

ON THE nature and scale of the menace, Daniel Pipes's **Militant Islam Reaches America** (Norton), sees the wider world as threatened by the violent outspill of a struggle for supremacy within Islam. He is less sanguine than Gilles Kepel, author of **Jihad: The Trial of Political Islam** (Harvard, I.B. Tauris), that the influence of anti-western fundamentalism has peaked. Owen Bennett Jones, in **Pakistan: Eye of the Storm** (Yale), focuses on one arena of that struggle within Islam. As to the wider consequences of September 11th, everyone will have a favourite and least favourite columnist. Thomas Friedman of the *New York Times* has the benefit of years of experience gathered in the Middle East. His **Longitudes and Attitudes** (Farrar, Straus & Giroux) comprises opinion pieces he wrote after September 11th

At the Edinburgh festival

Hit me hard

You need more than courage to make stand-up comedy out of Ground Zero

SEPTEMBER 11th dominated the Edinburgh fringe festival. Fresh-faced young Americans and middle-aged men brought the serious stuff: dramas about life-as-survival by an ensemble from the Playwrights Horizons' theatre school, life on a fire ladder as depicted by Tim Robbins and Susan Sarandon in "The Guys" and, inevitably a life-as-epic narrative by Steven Berkoff, fingers splayed and eyes popping as he artfully de-claimed his staged poem, "Requiem for Ground Zero".

All of which left life-as-art to irreverent, young non-Americans. Tina C, a British drag queen (pictured right), scorned entertainers who made money out of the tragedy. Mockery, as well as self-mockery, underlay her "Twin Towers Tribute" as she pouted across the stage poking fun at a nation's inability to



Feel the money, honey

comprehend why it is so widely hated. In "Behind Enemy Lines", an Anglo-Iranian stand-up comic, Omid Djalili, told jokes about terrorists and feeling paranoid. It was, in the end, a hit-and-miss effort. On stage, as elsewhere, it takes more than courage to land the perfect punch.

until June of this year. Agree or not, they make a readable guide to the issues and arguments facing American policymakers.

When war was declared on terror, many people asked who or what was the enemy. Two informative books on terrorism help sharpen the answer. **Combating Terrorism: Strategies of Ten Countries** (University of Michigan Press), a collection edited by Yonah Alexander, reminds us that the United States is not alone in facing this scourge, and compares experiences in counter-terrorism. David Whittaker's **Terrorism: Understanding the Global Threat** (Longman) is a clear and accessible survey of terrorist motives and methods, strengthened by several tables and a helpful chronology from 1968 to the present.

As terror is a psychological weapon of the weak used to undermine the self-confidence and authority of the strong, the psychological element in counter-terror is vital. Reminding yourself that your society and its values cannot be shaken is part of the war against terror: standing up for America matters. In this regard, do not be put off by the bragging title of Dinesh D'Souza's **What's So Great About America** (Regnery). Striking a middle path between left-wing multiculturalism and religious conservatism, he argues that America's founding originality was the separation of church and state, a beacon of toleration for the world.

For many non-Americans, the fact of American power alone is enough to explain why the United States should provoke such hatred. In **Why Do People Hate**

America? (Icon Books), Ziauddin Sardar and Merryl Wyn Davies provide a catalogue of American misdeeds and failings, real or imagined. It seems not to occur to them to ask whether, in fact, the world does hate America as much as they (and alas, too many Americans) suppose. A more balanced book on the urgent topic of Americans' and foreigners' misperceptions of each other is **The Eagle's Shadow** (Farrar, Straus & Giroux, Bloomsbury) by an American writer, Mark Hertsgaard, on why America fascinates and infuriates the world.

From a nation founded with a bill of rights, the voice of dissent is always stirring, irksome as it may be to democratic majorities and the powers that be. September 11th has thrown up two kinds of dissent, one worthless, one invaluable. The first, emanating chiefly from university English and cultural-studies departments, is a dissent of evasion or denial. **Dissent from the Homeland** (Duke University Press) is a lamentable example of self-styled social critics who have aestheticised politics and blinded themselves to the difference between death and its modes of representation. In vivid contrast are two well-informed sets of essays from the New Press in New York. **Understanding September 11** deals with Islamic radicalism, globalisation, terrorism, civil liberties and alternative viewpoints from a wide variety of authors, American and foreign. **Critical Views of September 11**, edited by Eric Herschberg and Kevin Moore, looks at the war on terror and related issues from a questioning vantage point. ■

New fiction

Letting go

The Lovely Bones. By Alice Sebold. Little, Brown; 328 pages; \$21.95. Picador; £12.99

TRAGEDIES are often dispatched in short order, and most of life is aftermath. Aptly for this month's gloomy anniversary, coming to terms with gratuitous violence and untimely death is what consumes Alice Sebold's affecting first novel, "The Lovely Bones". It has been a fiction hit in America all summer.

Raped and murdered by a misfit who has a habit of slaughtering young girls, 14-year-old Susie Salmon watches from a

pleasant, convivial heaven as her family grieves her loss and gradually makes peace with the fact that her murderer is never prosecuted. Susie's father so obsesses over the sinister neighbour he is certain killed his daughter—and he's right—that he becomes a pest to the police. Her mother seeks refuge in an affair with a detective, and literalises her need to put the murder behind her by deserting her husband and their remaining two children. Friends battle between clinging to Susie's memory and getting on with their lives.

Surprisingly, the conceit of looking down from heaven works nicely, since Ms Sebold avoids the precious, making Susie's paradise agreeably ordinary, a place where the dead learn to let go of the living while below the living learn to let go of the dead. The pervasive innocence of this novel will not appeal to all, but its direct,

open emotions are refreshing—and suitable to a 14-year-old's voice.

Susie sees her killer ride out local suspicions, and kill again. But her comprehension of what drives him is limited. A disturbed childhood with a shoplifting mother doesn't begin to explain his depravity. Just as well, too, for getting a grip on malice entails accepting the inexplicable: "Because horror on Earth is real and it is every day. It is like a flower or like the sun; it cannot be contained." Thus approaching human bloodlust as a natural phenomenon that people must live with like bad weather, Ms Sebold dramatises the Salmon family's halting, dogged healing without resort to a heart-tugging string section. However inscrutable she might find wickedness, equally enigmatic, as well as more compelling for her, is the improbable power to recover from it. ■

Bestsellers in America and Britain

What the world is reading

Almost anything but terrorism and Iraq

HOW will the anniversary wave of September 11th books fare in the bestseller lists? It may be early to judge. But the American non-fiction list contains as yet only a single title that touches on the topic, Jere Longman's "Among the Heroes", about the passengers on Flight 93 who fought back. Though the British non-fiction list in-

cludes two studies of second-world-war battles, there is nothing on either the terrorist attacks on New York and Washington or the ensuing war against terror.

Both fiction lists are, in fact, predictably light and end-of-summery, with plenty of big-name romance, crime and fantasy blockbusters. There are one or two exceptions, however, such as Alice

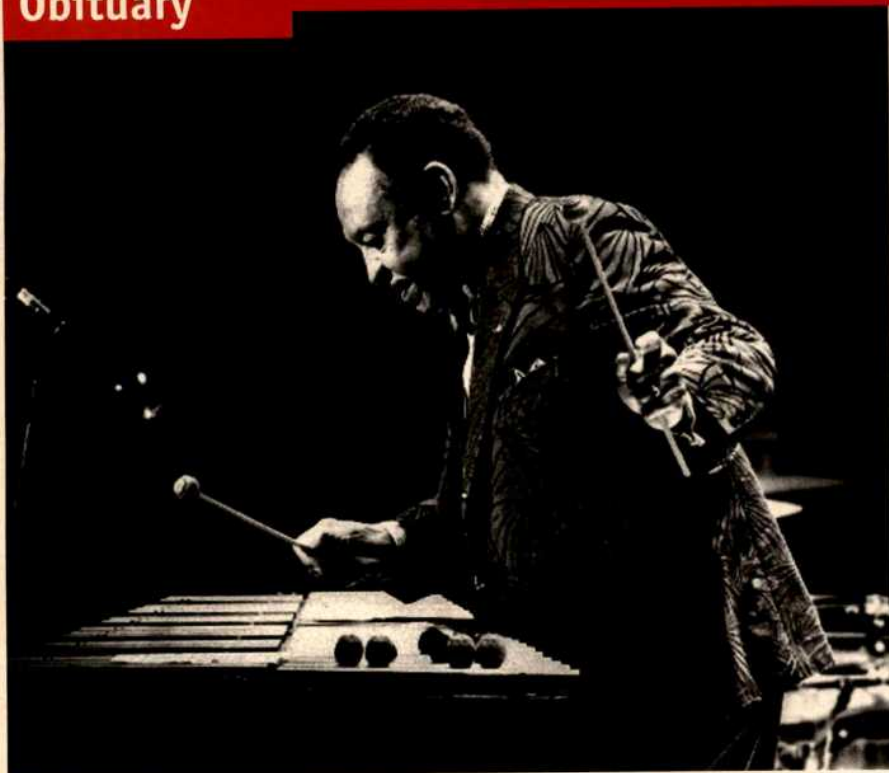
Sebold's "The Lovely Bones", whose popularity may reflect a post-September-11th mood in America (see review above), and the charmingly titled "Porno", Irvine Welsh's sequel to "Trainspotting". That said, if sex, drugs and ultraviolence are your idea of fun, perhaps "Porno" might be thought of as perfectly light and end-of-summery too.

Bestsellers

AMERICAN FICTION	AMERICAN NON-FICTION	BRITISH FICTION	BRITISH NON-FICTION
1 Red Rabbit by Tom Clancy Jack's back	The Perricone Prescription by Nicholas Perricone Lose those sags, bags and wrinkles	Porno by Irvine Welsh "Trainspotting" sequel	Cloughie: Walking on Water by Brian Clough Reminiscences of a football-club manager
2 The Lovely Bones by Alice Sebold The view from on high	Slander: Liberal Lies About the American Right by Ann Coulter In defence of Republicans	Quantins by Maeve Binchy Dublin restaurant docu-drama	One Hit Wonderland by Tony Hawks Global quest for a catchy melody
3 Standing in the Rainbow by Fannie Flagg Small-town, post-war yarn	Sacred Contracts by Caroline Myss What's your archetype?	Sunset in St Tropez by Danielle Steel Life's a pebble beach	Richard and Judy: The Autobiography by Richard Madeley and Judy Finnigan Talk-show team talk about themselves
4 The Nanny Diaries by Emma McLaughlin and Nicola Kraus Mary Poppins goes to Manhattan	Who Moved My Cheese? by Spencer Johnson Million-selling self-help fable	The Beach House by James Patterson and Peter de Jonge Death in the Hamptons	Inside "Big Brother" by Jean Ritchie Reality sound-bites
5 The Beach House by James Patterson and Peter de Jonge Death in the Hamptons	Self Matters by Phillip C. McGraw Looking out for number one	The Straw Men by Michael Marshall A funeral, a kidnapping, a raving lunatic	The Road to McCarthy by Pete McCarthy Myths of the McCarthys investigated
6 A Love of My Own by E. Lynn Harris Fast times at <i>Bling Bling</i> magazine	Body for Life by Bill Phillips Three months to total health	Grave Secrets by Kathy Reichs Getting forensic with Dr Temperance Brennan	Elvis Presley: Unseen Archives edited by Marie Clayton Anniversary tie-in
7 The Remnant: On the Brink of Armageddon by Tim LaHaye and Jerry B. Jenkins Apocalypse when?	Good to Great by Jim Collins The corporate X-factor	Land of Fire by Chris Ryan Back to the Falklands	Berlin: The Downfall 1945 by Antony Beevor Anatomy of a bloody victory
8 Eleventh Hour by Catherine Coulter FBI serial-killer thriller	Stupid White Men by Michael Moore What's wrong with America today	Beggars Banquet by Ian Rankin Short-story collection	Evelyn: A True Story by Evelyn Doyle Landmark child-custody case
9 Stone Kiss by Faye Kellerman From the City of Angels to Hell's Kitchen	The Right Words at the Right Time by Marlo Thomas Inspirational anecdotes	Stone Kiss by Faye Kellerman From the City of Angels to Hell's Kitchen	Serious: The Autobiography by John McEnroe He saw chalk dust
10 The Dive from Clausen's Pier by Ann Packer Lakeside melodrama	Among the Heroes by Jere Longman Commemorating courage on Flight 93	The Shelters of Stone by Jean M. Auel Fifth instalment in prehistoric saga	D-Day: June 6, 1944 by Stephen E. Ambrose Battle for the Normandy beaches

Sources: Publishers Weekly; Nielsen BookScan

Descriptions by The Economist



Lionel Hampton

Lionel Hampton, jazz musician, died on August 31st, aged 94

HAD this newspaper been running an obituary page at the time, Louis Armstrong, who died in 1971, would have been a natural choice. Duke Ellington (died 1974) and Bessie Smith (died 1937) are among others who would have made it. Lionel Hampton was of that flowering, and had the good grace to live to 94.

Until a few years ago he would still take to the stage with a band. Once at the piano or vibraphone, an electronic instrument he introduced to jazz, the marks of age would fall away and the sweaty passion that he had first brought to jazz back in the 1930s would be relived; and "Flying Home", his most famous composition, would soar for the hundredth, or perhaps the thousandth, time. Among the legends attached to "Flying Home" is that it depicts an American Flying Fortress bomber, damaged in a raid over Germany, with its crew urging on the aircraft as it strives to reach its base in eastern England. Listening to a recording of the number made during the second world war, with Mr Hampton's driving solos and his grunts of excitement as the pace quickens, it does seem to convey a will to win.

Never mind that "Flying Home" was written before the Americans went to war in 1941; Lionel Hampton, like Glenn Miller, provided much of the background music

to the war. The young men and women who danced to his music until the floor creaked danced just as energetically when they went into uniform. Their children and grandchildren are still dancing to the derivative music of bands such as the Rolling Stones. Who invented rock and roll is an unsettled argument, but Mr Hampton had a hand in it. Perhaps because of his association with one of the more limited offshoots of jazz, the range of his gifts may have been overlooked.

The "beat in me"

At the age of six Lionel Hampton discovered what he called the "beat in me" while attending church in Alabama, where the congregation clapped along with a guitarist and other performers. What distinguishes the beat in jazz is that it is slightly delayed. It makes jazz sound relaxed. However many decibels Mr Hampton produced, however much excitement he generated, however much pandemonium he created on the dance floor, there was always in his music the delayed beat that underpins much of great jazz.

It is especially distinctive in a number of records he made with Benny Goodman. Although Goodman ran a successful swing band, he is remembered by connoisseurs for his quartet in which Mr Hampton

played the vibraphone with melodic simplicity. Remarkably for the time, the group was racially mixed: Lionel Hampton and Teddy Wilson, the pianist in the quartet, were black. As his fame grew Mr Hampton was courted by politicians after the black vote. Harry Truman, a Democrat, was a fan and got Mr Hampton to play at his presidential inauguration. But Mr Hampton favoured the Republicans: unlike the Democrats, he said, Republicans helped blacks "without ballyhoo".

The Republicans were pleasantly surprised. Mr Hampton was undoubtedly an asset to the party that sees itself as the promoter of self-reliance. He had learnt the rudiments of music from a nun at a boarding school where he was placed after his father was killed in the first world war. He worked as a newspaper seller to pay for tuition at a music school. By his late teens he was a professional musician in Chicago, playing piano, vibraphone and drums. Chicago was then the country's main jazz city, where Armstrong recorded "West End Blues", considered by some to be America's finest piece of music, jazz or classical. Mr Hampton worked for a while with Armstrong, as he did with most jazz musicians over the next 50 years, many of whom, such as Dizzie Gillespie, became famous as innovators. Mr Hampton remained a conservative in his musical style. "All those altered scales and harmonic extensions people were calling modern in the 1940s, I knew all about years earlier," he said.

He was conservative too in his life off-stage. Unlike musicians who blew their money and their minds on drink and drugs, Mr Hampton was a careful saver. He owned a record company and several blocks of flats in New York's Harlem district. He set up scholarships in music schools. Academe rewarded him with a dozen honorary doctorates. One of his vibraphones is in a Washington museum, along with Goodman's clarinet.

Mr Hampton became head of a group called Black Republicans. He campaigned for, among others, Richard Nixon, Ronald Reagan and George Bush, senior. After they were elected they sent Mr Hampton on world tours to promote American culture. The Germans especially appreciated his concerts. There is a road in Berlin called Hamptonstrasse.

Big-time politics was a temptation. He served on New York's Human Relations Commission and could perhaps have made it to Congress. The politician in him said, "I always liked to be taking bows." But he was getting old. It was music, rather than the slog of politics, that made him feel young again; with the mallets falling on the vibes and the driving rhythm that got the crowd going. "Flying Home". One more time. ■

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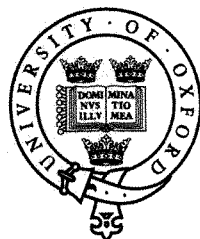
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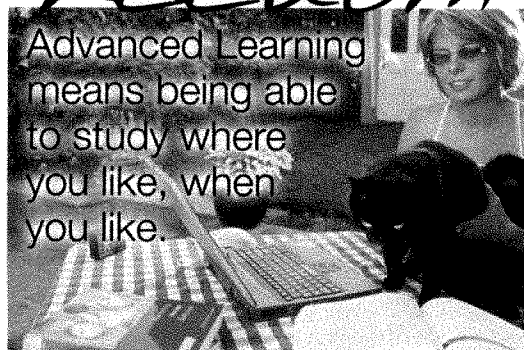
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- Administration of tendering procedures, particularly publication of procurement notices, establishing tender dossiers, organisation of evaluation committees
- Participation in evaluation committees as chairman
- Advice on legal issues e.g. claims and litigation.

Job Profile: See general introduction.

Candidates must have:

- University degree in law
- At least three years professional experience in contracting
- Specialisation in international commercial law, public/private international law, public administration, FIDIC contracting conditions, knowledge of tender procedures would be advantageous
- Knowledge of other European or local languages are also an advantage
- The contract lawyer is a reliable and responsible personality and must be able to work flexibly under demanding professional circumstances and in an international atmosphere
- The contract lawyer needs to be a team player while being independent and able to work autonomously
- She/he will be able to work in difficult living and working conditions involving also travelling in the region.

Applications including a detailed Curriculum Vitae, and an e-mail cover note which should also indicate the job reference number, should be sent by e-mail only, and in English only, to: adm@ear.eu.int

The Agency is an equal opportunity employer, and encourages applications from women.

Applicants will be short-listed on the basis of their CVs, and short-listed candidates will be invited for an interview.

Candidates who have not been contacted by 31st October 2002 should consider that there will be no follow-up to their application.

Deadline for the submission of applications: 30th September 2002



Team Leader-

Marine Biodiversity Conservation Project Milne Bay, Papua New Guinea

Conservation International, in conjunction with The United Nations Development Program, and The Global Environmental Facility, seeks a Team Leader (TL) for a multisectoral marine biodiversity conservation program in Milne Bay, PNG. The TL (to be based in Alotau) will be the senior on-site officer, and will coordinate the overall implementation of the Milne Bay Community-Based Coastal and Marine Conservation Project. Initial 2-yr contract has potential to be extended to 5-year life of project. The TL will ensure the project's delivery of outcomes and impacts, as well as capacity building within Provincial Government Administration, leading to government assuming project administration. The TL is also responsible for technical inputs toward project development, actual project outputs/impacts, project reporting, reviews and appropriate site monitoring (travel by small boat over open seas).

Responsibilities:

- Lead staff and Govt/NGO partners in project design and adaptive management
- Direct all project reporting for Project Steering Committee, Review Meetings, annual work plans, etc.
- Manage technical inputs, project outcomes, reviews, monitoring, and facilitate workshops
- Direct international and national consultants/contractors to ensure technical quality
- Communicate lessons learned through knowledge-sharing networks to aid design of other projects

Requirements:

Relevant degree (Masters preferred); superior record managing international programs; 15+ years in environmental conservation; experience with Melanesia and marine conservation is desirable; also desirable are substantial management knowledge in alternative livelihoods, subsistence improvement, biodiversity conservation, marine systems evaluation, and multisectoral project management; Fluency in English, an adaptive management style, and familiarity with international project management rules and regulations are required, as are good coordination and negotiation skills. For complete Terms of Reference and related documents visit website:

http://www.conservation.org/xp/CIWEB/about/jobs/Melanesia_team_leader_MBCP.xml

This position is open to applicants of all nationalities. Women are encouraged to apply. Interested candidates should pay close attention to the selection criteria and send their documents on e-mail by 7th October 2002, to: (email) ci-moresby@conservation.org or on diskette to: Conservation International, Box 106 Waigani, NCD, PNG. Include a cover letter and a CV of no more than 5 pages. Your CV must address this ad's selection criteria (duties & responsibilities). Provide contacts for 3 referees with recent experience supervising your work. No calls or office visits. Do not send other documents or certificates. Only candidates to be interviewed will be contacted.



(ICRC), an independent humanitarian organisation whose mandate is to provide protection and assistance for victims of armed conflict and internal disturbances, has a vacancy at its headquarters in Geneva for a

Legal Adviser

Advisory Service in International Humanitarian Law (IHL)

male or female (100%)

Purpose of the post and responsibilities :

To contribute to the ICRC's efforts in the field of national implementation of IHL, in particular in providing technical assistance to governments of common law countries in the promotion of ratification of humanitarian law treaties and in the adoption of national legislation to implement the treaties at the national level.

To promote the establishment of national committees for the implementation of IHL and provide technical assistance to existing committees.

To organise and to participate in seminars, courses, conferences on topics related to IHL and its implementation.

To supervise and to co-ordinate the work of regional legal advisers based in ICRC delegations covering common law countries to participate in the establishment of the priorities of the Advisory Service world-wide.

Training and experience required :

Lawyer trained in common law system with a specialisation in IHL and experienced in working with governments.

Please refer to our web site "www.icrc.org", under the topic "job at ICRC" for further information and application if you are interested.

United Nations Development Programme

Electricity Network Development Programme Northern Iraq



VACANCY ANNOUNCEMENT

Post Title: Chief Technical Manager (CTM)
Post Number: TECH/02/004
Duration: 6 months, renewable
Duty Station: Northern Iraq (non-family duty station)

Within the framework of the Programme of the Humanitarian Assistance to Iraq, UNDP has been entrusted with the rehabilitation of the electricity network in the three Northern Governorates, under Security Council Resolution 986. The Programme is being funded by the 'Oil for Food' mechanism and to date, approximately US\$997 million has been allocated to the rehabilitation of the electricity network in the three Northern Governorates.

The Technical Section, as part of the Central Programme Office is headed by the CTM and is organized into five sectors, responsible for generation, transmission, substations, distribution and operations & maintenance. Each sector is managed by a Sector Manager who reports to the CTM.

The candidate would be expected to possess a university engineering degree in a related field and a minimum of 20 years work experience in the electricity sector. Knowledge and experience in the operation of an electricity network, overseas experience and management skills would be indispensable assets.

The complete Terms of Reference are available on the ENRP website: www.enrp.undp.org. UNDP will negotiate with the successful candidate and enter into a contract specifying the remuneration and employment conditions.

Applications with clear indication of "post number" applied for should be submitted by fax or e-mail by **30 September 2002** to:

Attn: Sabina Mascarenhas
Personnel Specialist
UNDP/ENRP-Erbil
Northern Iraq
Fax No.: 001 212 963 4793 or
001 212 202 6387
E-mail: personnele@un.org

Water and Wastewater Project Opportunities Project Management, Sales, Engineering, Construction and Utility Financial Management

Central & Eastern Europe, Central Asian Republics and the Middle East

CH2M HILL is one of the largest water and wastewater planning, engineering, design, construction and operations companies in the world with over 12,000 employees and over US\$ 2 billion in annual turnover. We are currently planning to expand our existing operations in the pre-accession countries of Central and Eastern Europe and in the Middle East and the Central Asian Republics. CH2M HILL seeks talented, experienced and entrepreneurial management-level personnel for positions in water resources, water treatment and wastewater treatment projects.

The following positions are available:

Construction Manager

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Industrial Wastewater Manager - West Bank

Senior Project Manager - Conventional and/or Design Build

Water / Wastewater Utility Financial Management

In addition, we have significant global career opportunities for experienced Project and Program Managers in Southeast Asia, Australia, China, Brazil, USA and Canada.

The preferred candidates would have a professional degree; at least 15 years international EPC water resources, water treatment and/or wastewater treatment project experience, preferably in emerging or developing countries and preferably on international financial institution (WB, EBRD, ISPA/PHARE, USAID) funded projects; strong English language and communication skills, multi-cultural sensitivity and flexibility, and superior people management skills. Candidates should indicate their current citizenship and salary requirements.

CH2M HILL, a global project delivery company, is an employee-owned firm and an equal opportunity employer. We are deeply committed to employee development and becoming a benchmark learning corporation. We provide personnel with support, tools and processes they require so that projects exceed our clients' expectations.



CH2MHILL

Please forward your CV to:

Mike West, Manager of Global Recruiting at:
waterpmcm@ch2m.com or contact directly on 303 874 3085.
Principals only, no executive search firm submittals.



NUFFIELD COLLEGE OXFORD

Official Fellowships in Sociology

The College proposes to appoint, with effect from 1st January 2003, or as soon thereafter as may be convenient, two Official Fellows in Sociology. Official Fellowships are comparable with tenured research Professorships; holders are expected to supervise doctoral students, but have no course or lecturing obligations. Nuffield College is a social science graduate institution, within Oxford University, with a strong research tradition of empirically informed and theoretically aware sociology. It is expected that the new appointments will strengthen that contribution to sociology. There is no restriction on substantive field.

Salary on a scale rising to £56,635 p.a. generous research allowance; details from the Warden's Secretary, Nuffield College, Oxford OX1 1NF, UK (e-mail: sociology.fellowship@nuffield.ox.ac.uk) or at www.nuff.ox.ac.uk Applications should be received by 30th September 2002.

The College exists to promote excellence in social science research and graduate education.

Nuffield College is an equal opportunities employer.

United Nations Development Programme

Electricity Network Development Programme
Northern Iraq



VACANCY ANNOUNCEMENT

Duration: 6 months, renewable
Duty Station: Northern Iraq (non-family duty station)

Within the framework of the Programme of the Humanitarian Assistance to Iraq, UNDP has been entrusted with the rehabilitation of the electricity network in the three Northern Governorates, under Security Council Resolution 986. The Programme is being funded by the 'Oil for Food' mechanism and to date, approximately US\$997 million has been allocated to the rehabilitation of the electricity network in the three Northern Governorates.

INDIVIDUALS

The Programme invites individuals with suitable experience to apply for the following senior technical positions.

TECH/02/005	Sector Manager Distribution	One Position
TECH/02/006	Sector Manager Generation	One Position
TECH/02/007	Sector Manager Substations	One Position
TECH/02/008	Deputy Sector Manager Substations	One Position
TECH/02/009	Deputy Sector Manager Distribution	One Position
TECH/02/010	Manager Operations and Maintenance	One Position

CONSULTANTS

The Programme also invites consulting companies to submit names and CVs of qualified candidates and experienced consultants for the following positions (INDIVIDUAL CANDIDATES NEED NOT APPLY).

TECH/02/001	Electrical Engineer Hydro	Two Positions
TECH/02/002	Mechanical Engineer Hydro	One Position
TECH/02/003	O&M Engineer - Large Diesels	One Position

The INDIVIDUAL candidates would be expected to possess a university engineering degree in a related field and a minimum of 20 years work experience in the electricity sector. Knowledge and experience in the operation of an electricity network, overseas experience and management skills would be indispensable assets. CONSULTANTS should have adequate qualifications and experience in their respective fields of expertise.

The complete Terms of Reference for each position are available on the ENRP website: www.enrp.undp.org. UNDP will negotiate with successful candidates and consulting companies and enter into contracts specifying the remuneration and terms and conditions.

Applications with clear indication of "post number" applied for should be submitted by fax or e-mail by 30 September 2002 to:

Attn:	Sabina Mascarenhas Personnel Specialist UNDP/ENRP-Erbil Northern Iraq	Fax No.:	001 212 963 4793 or 001 212 202 6387
		E-mail	personnele@un.org

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National University of Ireland, Galway
Ollscoil na hÉireann, Gaillimh

J.E. CAIRNES PROFESSORSHIP OF ECONOMICS (Half-Time)

The Department of Economics wishes to invite applications for the above post. In filling this post, the Department wishes to develop particular expertise in the following areas: Computable Economics, Non-Linear Dynamical Modelling, and Behavioural Economics. The candidate will be an established researcher of international standing in one or more of the above areas. The successful candidate will lead the development of these research areas in the Department and provide a teaching input to its graduate programmes. He/she will also contribute to an interdisciplinary research group on modelling systems within the University.

Further information on the post and the Department of Economics may be obtained from:

Professor Michael Cuddy,
Tel.: +353-91-750324; Fax: +353-91-524130
Email: michael.cuddy@nuigalway.ie
or from the Department of Economics Web Page at:
www.economics.nuigalway.ie

Further information is available from the Personnel Office website:
www.nuigalway.ie/news

Candidates should submit six copies of their Curriculum Vitae with the names and addresses of at least three, and not more than five referees to:

The Personnel Office,
National University of Ireland, Galway, Ireland.
Tel: +353-91-512069; Fax: +353-91-750523
Email: personnel@mis.nuigalway.ie
Website: www.nuigalway.ie/news

Closing date for receipt of applications is **Friday, 11th October, 2002.**
National University of Ireland, Galway is an equal opportunities employer.

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The University of Erfurt, Germany, invites applications for a

Chair in Family Sciences

The ideal candidate has published theoretical or empirical research in international journals.

Deadline for applications: 30 September.

For further information e-mail
ulrike.engelbert@uni-erfurt.de

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A career in the heart of Europe



The EIB, the financing institution of the European Union, is currently seeking for its **Projects Directorate, Industry & Services Department, Primary & Intermediary Materials and Life Sciences General Secretariat, in Luxembourg a (m/f)**

Industrial Economist

The Project Directorate is responsible for the technical, economic and environmental appraisal of projects. Formed of multidisciplinary teams of engineers and economists, the Directorate is organised by sector. It supports lending activities in Europe and throughout the world.

Responsibilities: Assessment of the economic viability of capital investment projects and programmes in the Primary & Intermediary Materials, Life Sciences and related Service sectors. As part of a multidisciplinary team, the Economist will:

- Assess the economic, financial and environmental viability of investment projects and programmes in the relevant industrial and service sectors in the EU Member States, the EU Accession Countries and in other countries worldwide where the Bank operates. The main sectors covered are primary resources and process industries, life sciences, including biotechnology, and related services. An increasing focus is expected on intangible investment related to the knowledge based economy e.g. R&D, training, e-commerce.
- Promote the understanding of the sectors of his/her responsibility within the Projects Directorate and the Bank and maintain contacts with outside networks, including the Commission and other international bodies concerned with these sectors.
- Prepare methodology and market studies and policy papers related to the sectors of his/her responsibility to identify business and lending priorities.
- Closely cooperate with the Lending Directorates and assist in the identification of investment opportunities.
- Monitor the implementation of financed investments.

Qualifications: Relevant academic qualifications in economics, preferably with a specialisation in industrial economics or the economics of the firm. A minimum of 3 years experience gained in the assessment of projects in the corporate, consultancy or financial sectors, with exposure to market analysis. Experience of applied quantitative methods, economic and financial modelling, including modern valuation methods, cost-benefit analysis, risk analysis and environmental impact assessment. Given that an increasing share of the Bank's industrial operations are located in the EU Accession and associated Mediterranean and overseas countries, experience in these geographic areas will be valuable. Excellent knowledge of **English or French** and a good command of the other. Working knowledge of other EU languages would be an advantage.

Skills:

- Good interpersonal, team-working and communication skills.
- Good analytical and reasoning skills with capacity to provide sound judgement concerning the issues in his/her areas of responsibility.
- Ability to operate in international environments, including those of developing countries.
- Knowledge of the preparation and review of feasibility studies.
- Judgement concerning the issues in his/her areas of responsibility.
- Ability to operate in international environments, including those of developing countries.
- Knowledge of the preparation and review of feasibility studies.
- Capacity to plan and organise his/her work and to work under pressure.
- Ability to draft clear and concise reports.
- Results-orientated.

Applicants must be **nationals of of a Member Country of the European Union or of an Accession Country**. The EIB offers attractive terms of employment and remuneration with a wide range of welfare benefits. **It is an Equal Opportunities Employer and particularly welcomes applications from women.**

Applications should include a cover letter **quoting the relevant reference number** and a curriculum vitae in **English or French** and be sent to:

EUROPEAN INVESTMENT BANK, Staffing Division (Ref. PJ02ECO05)
L-2950 LUXEMBOURG. Fax: +352 4379 2545. E-mail: jobs@eib.org

Applications will be treated in strictest confidence.

They will not be returned. Personal data are protected by Community Regulation.

For further particulars about the EIB, its remits and how it operates, visit the EIB's website: <http://www.eib.org>

Programme Manager

Natural Resources Systems Programme, UK



HTS Development Ltd is a leading UK based Development Consultancy. Under contract to the UK Department for International Development (DFID), we are managing the Natural Resources Systems Programme (NRSP). As one of DFID's ten natural resource (NR) programmes, NRSP undertakes research on the integrated management of natural resources with a central goal of delivery of new knowledge that can enable poor people who are largely dependent on the NR base to improve their livelihoods. Further information can be obtained at: www.nrsp.co.uk

We are seeking applications from National Senior Research Scientists with a higher degree in natural resources or relevant field and at least 10 years experience in research management, including significant experience in the developing world. Knowledge of DFID procedures would be an advantage.

The Programme Manager will be based in the UK at our head office and have overall responsibility for programme implementation through commissioned projects and contracted assignments for promotion of research products, budget control, coordination of management and projects teams and supervision of administrative and financial matters. Applicants should be nationals of the European Economic Area.

Closing date for applications is 30 September 2002.

Send CV and covering letter quoting **Ref NRSP/02** to:

Sue Adams, HTS Development Ltd,
Thamesfield House, Boundary Way,
Hemel Hempstead, Hertfordshire, HP2 7SR.

Phone: 44 1442 202440

Email: sue.adams@htsdevelopment.com

INTERNATIONAL EDUCATION TEAM LEADERS AND CONSULTANTS



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Brisbane QLD 4001
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TEL:
61 7 3859 1500

WEBSITE:
www.grm.com.au

GRM International Pty Ltd is one of Australia's leading resource management groups with over 30 years experience in international development and project management. We currently manage a number of significant education, capacity building and institutional strengthening projects on behalf of the World Bank, ADB and AusAID.

We are seeking expressions of interest from education practitioners with significant domestic and/or international experience for current and upcoming projects in PNG, South Africa and the Pacific.

Opportunities exist for both long-term and short-term consultancies in the following areas:

- Educational Capacity Building and Reform
- Basic Education
- Curriculum Development
- Teacher Development and Training
- Bilingual Literacy and Linguistics
- Transition Programs
- Construction and Maintenance of Educational Infrastructure
- Distance Education
- Procurement and Logistics
- Community Skills Development in Education
- Gender Equity and Development in Education

Persons with team leadership, project management, project design and monitoring and evaluation experience are strongly encouraged to express interest. For further information and details of current opportunities please refer to the company website.

Expressions of interest together with a current curriculum vitae are to be submitted to Simon Kutcher by 20th September 2002 by email



ASSOCIATION FOR WOMEN'S RIGHTS IN DEVELOPMENT WOMEN'S RIGHTS AND ECONOMIC CHANGE THEME MANAGER

AWID is an international membership organization connecting, informing and mobilizing people and organizations committed to achieving gender equality, sustainable development and women's human rights. Our diverse membership includes educators, activists, business people, policy-makers, development practitioners and funders. Our goal is to cause policy, institutional and individual changes that improve the lives of women and girls everywhere.

Our Programs:

AWID's International Forum on Women's Rights and Development: Reinventing Globalization. Known as the largest recurring international summit on gender equality outside of the United Nations, AWID's Forum is a unique opportunity for the women's movement to assess our work and forge new strategies. On October 3-6 2002, hundreds of our members will convene in Mexico to "reinvent globalization" for women's rights and development. **The Strategic Communications Program** aims to provide practical and accessible multi-perspective information to our diverse membership.

Goals of the Theme Manager: a) building the capacity of gender equality advocates to understand the processes of globalization; b) developing viable policy recommendations, economic alternatives and approaches that ensure gender and economic justice; c) influencing international financial and private sector institutions, national governments and civil society to ensure that new gender-sensitive ideas are translated into concrete outcomes. At the heart of this theme is the belief that working towards a global economic system in which rights are guaranteed requires close collaboration between the fields of women's human rights and economic development. AWID's secretariat is located in Toronto, Canada. We encourage individuals from and living in the global South or Eastern & Central Europe to apply. The theme manager will work from their current location.

Qualifications:

- Post-graduate studies in economics with a gender focus or 5 yr minimum work experience in gender equality and economics that includes communications outputs;
- Proven commitment to gender equality;
- Experience working independently and under pressure; self-motivated;
- Excellent written and oral communication skills (English, other languages an asset);
- Superior interpersonal, cross-cultural and collaborative skills;
- Proficient in Microsoft Word and Excel.

To Apply, send: a) your Curriculum Vitae, b) 2-3 pages describing your recommendations to guarantee women's rights in the context of globalization; and c) a 1-2 pg unedited writing sample to:

Association for Women's Rights in Development
Re: Women's Rights and Economic Change Manager
96 Spadina Avenue, Suite 401, Toronto, ON, M5V 2J6, Canada
Fax: 416-594-0330 / email: hrrwec@awid.org / <http://www.awid.org>
* Only shortlisted candidates will be contacted.



COMMON MARKET FOR EASTERN AND SOUTHERN AFRICA (COMESA) PROJECT MANAGER \$48,000 p.a.

The Common Market for Eastern and Southern Africa (COMESA) was set up in 1994 replacing the Preferential Trade Area (PTA) which was established in 1981. The COMESA Treaty envisions a fully integrated, internationally competitive regional economic community that can facilitate sustainable economic development, social and political stability in the region.

Globalisation and the WTO trade liberalisation programme are imposing new challenges on COMESA members and the region as a whole. These countries face new obligations in terms of enabling domestic legislation, commitments on notification and administrative adjustments. The countries are facing an expanding programme of trade negotiations at regional and global levels.

COMESA has secured funding from the African Capacity Building Foundation (ACBF) to implement a four-year project to strengthen capacity for trade negotiations and trade policy development and management within eastern and southern Africa.

The project has the following specific objectives:

- a) Strengthening COMESA Secretariat in trade negotiations, trade policy and management skills including policy issues relating to the establishment of a customs union
- b) Supporting COMESA member states in the area of trade negotiations, trade policy and management at regional and international level
- c) Reinforcing private sector and civil society participation in trade policy, regional and global integration issues.

Description of Duties:

Under the guidance of the Project Steering Committee and immediate supervision of the Assistant Secretary General, the incumbent shall:

1. Prepare a four year implementation plan and budget for the project
2. Conduct a skills gap and training needs assessments for Secretariat and member states.
3. Design and organise training programmes for staff of the Secretariat and member states
4. Organise joint workshops for the private sector, the public sector and civil society organisations on issues related to trade as well as regional and international integration
5. Develop performance indicators and monitoring tools to evaluate implementation progress
6. Prepare annual work programmes, budgets and quarterly reports
7. Prepare accounts for audits and other evaluations as required
8. Establish and oversee the day-to-day management and implementation of project activities
9. Participate in COMESA meetings, prepare papers and positions
10. Interact with COMESA Ambassadors in Geneva

Qualifications

The post suits an energetic, self-motivated national of any African country who is able to work under a variety of situations. Attributes looked for in such an individual are:

1. Postgraduate qualification in a suitable discipline
2. At least ten years experience in the field of regional and international trade
3. Sound knowledge of trade related issues, particularly as they pertain to policy development and management, integration as well as negotiations
4. Demonstrated capability in project management with particular emphasis on capacity building and skills training
5. Experience in a multi-national environment will be an added advantage
6. Ability to communicate effectively in English and French is desirable

Applications

Please apply to: The Secretary General, COMESA Secretariat, P O Box 30051, 10101 Lusaka, Zambia.
Fax + 260 1 225107. Applications can also be made by E-mail to: secgen@comesa.int.
Applications should reach the Secretariat by 30th September 2002.



ÉCOLE POLYTECHNIQUE
FÉDÉRALE DE LAUSANNE



Faculty Positions in Management of Technology

The Swiss Federal Institute of Technology in Lausanne and the Faculty of Economics of the University of Lausanne (UNIL-HEC) invite applications for four Faculty Professor positions (assistant, tenure-track, associate or full) in Management of Technology to build up a strong core team for a newly created joint centre.

We seek highly qualified individuals committed to a career in research and teaching, with an interdisciplinary vision and a strong record of accomplishments in one or several of the following areas:

- Strategy and organisations
- Strategic change, innovation management and intra/entrepreneurship
- Logistics and information systems
- Industrial economics and competitive strategies
- Technology management and risk assessment
- Operations management and technology

The successful candidates are expected to participate in EPFL's and UNIL-HEC's joint research and teaching activities in the fields of Management of Technology more specifically related to strategy, research and development, innovation and emerging technology.

The centre will develop and manage undergraduate, graduate (doctoral) and various master programs. It will also develop collaborations with the private and the public sectors.



Deadline for application:
October 15, 2002.

Please send letter of interest, current CV, and the names, phone numbers and e-mail addresses of at least five reference persons to:

Prof. Francis-Luc Perret, EPFL
Chairman of the Search Committee
CH-1015 Lausanne, Switzerland

EPFL:
<http://ilemt.epfl.ch/>
Prof. F.-L. Perret

UNIL-HEC:
<http://www.hec.unil.ch/>
Prof. A. Bergmann

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SOFRECO A leading French consulting firm is urgently seeking:

7 LONG-TERM EXPERTS - REPRODUCTIVE HEALTH - TURKEY

Positions & Qualifications:

- **Team Leader:** 5-10 years experience in reproductive health projects' management;
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- **CSO/Capacity Building Expert:** 10 years working with a CSO + 5 years training in multi-donor settings;
- **Financial Management and Procurement Expert:** 10 years experience;
- **2 Field Officers:** 5 years working with a CSO + Turkish-speaking.

Job Requirements:

- EU or MEDA nationals;
- University degree (Master's level if possible) in the relevant field;
- Minimum 5 to 10 years experience in the required field of expertise and in international projects;
- Excellent management, interpersonal, communication, organisational, planning, problem-solving, leadership abilities and a high degree of personal initiative;
- **Fluency in English;**
- Would be assets: - Knowledge of EC procedures; - Turkish-speaking; - Experience in gender and cultural issues in developing countries.

These are full time positions for 4 years with a possible 1-year extension.
Copies of diplomas and work certificates will be required. Detailed job descriptions upon request.

Send CV to: health@sofreco.com, with reference OH2695.

The Economist September 7th 2002

Announcements

HUNTINGTON BOOK PRIZE

The students and friends of Samuel P. Huntington have established a \$10,000 prize for the best book published each year in national security studies. The book can be a work of history or political science or a work by a practitioner of statecraft.

Nominations for books published in 2002 will be accepted until January 31, 2003. The winner of the 2002 prize will be announced May 1, 2003. Send nominations and two copies of the book to:

Ann Townes
The Olin Institute for Strategic Studies
1033 Massachusetts Avenue
Cambridge, MA 02138

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E-mail: helen@scfgroup.com E-mail: janson@scfgroup.com
Charles Baker M.A. (Hons)
E-mail: charles@scfgroup.com

Tenders

Health Resource Centre

(Communicable Disease, HIV/AIDS, Sexual, Reproductive, Maternal and Child Health)

Scope of Work

To support its strategy for improving the health of poor people DFID is seeking Expressions of Interest (EOI) from consortia to operate a Resource Centre for Communicable Disease, HIV/AIDS, Sexual, Reproductive, Maternal and Child Health. It will absorb the functions of two existing resource centres – the Sexual and Reproductive Health Resource Centre and the Malaria Consortium, expand their functions and be expected to work closely with other resource centres, to meet cross-cutting demands. DFID will pay particular attention to EOIs setting out arrangements to facilitate this way of working.

The Resource Centre will maximise use of developing country institutions and regional expertise, build local capacity and provide a high and increasing proportion of consultants from developing countries. It will demonstrate proven competence in the above fields and health systems. There will be a contract for core services and a Framework Arrangement. Separate call-down contracts will be issued at short notice to engage individuals or small teams as and when required. There is no obligation on the part of DFID to use the services offered under the Framework Arrangement. The service provider will not be eligible to implement work, which it has designed, unless commissioned at the outset.

It is envisaged that the contract will be for a period of 3 years commencing in January 2003. Subject to satisfactory performance, there may be the possibility of an extension of a further 2 years.

Draft Terms of Reference are available at
www.dfid.gov.uk/contracts/contractopportunities.asp

Details of DFID's strategy for improving the health of poor people can be found at http://www.dfid.gov.uk/pubs/files/tsp_health.pdf

Qualifications

Applicants should demonstrate evidence of capability, skills and experience in the following areas:

(i) Good understanding of development principles (including the Millennium Development Goals and other key international development targets) and DFID strategies, with an emphasis on positive outcomes for the poor, equity, ownership, sustainability and learning. Experience of working with developing country governments through sector-wide approaches and poverty reduction strategies;

(ii) Technical experience, track record and capacity in the fields of communicable disease, HIV/AIDS, sexual, reproductive, maternal and

child health in OECD and developing countries, and demonstrable access to a broad international pool of high quality consultants and experts including through "virtual" networking;

(iii) Excellent management skills, including business planning and management of consultants, projects and programmes, process-based work (including managing change) and demonstrable skills in interdisciplinary working;

(iv) Developing country institutions demonstrably involved in consortia. At least one institution should be from Africa and one from Asia;

(v) Knowledge and communications. The ability to identify and link closely with relevant research, summarise it into practical guidance, and support its practical application. Also to develop links to disseminate such information widely;

(vi) Capacity Development. Skills and experience in facilitating North-South and South-South exchange and learning;

As well as demonstrating evidence of the above, applicants should also provide evidence that their business has been trading for at least 5 years.

Expression of Interest

The Expression of Interest must be in the form of a Capability Statement, of not more than four A4 pages, be accompanied by abridged CV's of key personnel and include a Statement of the firm's overall turnover and the turnover in respect of the services to which the contract relates for the three previous financial years. Following assessment of the EOIs, DFID will invite short-listed applicants to submit full technical and commercial proposals. Prices are not required at this stage, however when required, prices must be in Sterling and all payments under the contract will be made in Sterling. The contract will be governed by English law. DFID reserves the right to annul the tendering process and not to award the contract.

This request for EOIs is also advertised in the supplement to the Official Journal of the European Communities.

EOIs must be submitted to Steven O'Raw (cb5mail@dfid.gov.uk), Room AH409/2, Department for International Development, Abercrombie House, Eaglesham Road, East Kilbride, Glasgow, G75 8EA to be received no later than 14:00 on Thursday 10th October 2002. Please quote reference no EOI 02 4103.

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Tenders



National Highways Authority of India

(Ministry of Road Transport and Highways)

**GLOBAL REQUEST FOR EXPRESSION OF INTEREST
FROM REPUTED FIRMS FOR PROVIDING SMART CARD
TECHNOLOGY FOR TOLL COLLECTION SYSTEM AT
VARIOUS LOCATIONS ON NATIONAL HIGHWAYS**

- National Highways Authority of India intends to start use of Smart Cards for toll collection at its various Toll plazas located on National Highways entrusted to NHAI. Experienced Firms/Joint Ventures are hereby invited to submit their 'Expression of Interest' for providing total solution for the use of Smart Cards on Toll plazas. The total solution must consist of the following:
 - Inter-operability of Smart Cards.
 - Proposed appropriate technology, memory and system requirements.
 - Back-end arrangements for near real time distribution amongst different operators, according to the actual proceeds.
 - Making toll collection system secure through adequate key management system.
 - Option of integration of Smart Cards for other road related facilities like wayside amenities/petrol pumps, etc.
- The interested Firms are required to give the following information in their 'Expression of Interest':
 - Structure and organisation of the Firm :
 - Type of work done.
 - Country and year of incorporation.
 - Annual turnover for the last 5 years.
 - Experience in providing systems for use of Smart Cards.
 - Present workload, number and type of similar assignments.
 - A model on proposed solution covering all the features enumerated in para 1.
- Interested Firms may obtain further information from the address given below.
- 'Expression of Interest' must be delivered to the address mentioned below by 1600 hrs on 30 September, 2002.

This notice is also available on NHAI's Website <http://www.nhai.org>
Address for Communication:
General Manager (Corridor Management),
National Highways Authority of India,
G - 5 & 6, Sector - 10, Dwarka, New Delhi - 110 045, India.
Ph.: 91-11-5074200 Extn: 1408. Fax: 91-11-5093507/5093514.
E-mail : nhai@vsnl.com Website : <http://www.nhai.org>

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Overview

Stockmarkets tumbled, on jitters about a possible war against Iraq and worries about the faltering recovery in rich countries. On September 3rd, the S&P 500 saw its biggest one-day fall since last year's terrorist attacks. Over the week it declined by 2.7%, while the Dow Jones Industrial Average fell by 3.1%. Europe's stockmarkets dropped even more sharply. France's CAC 40 fell by 7.3%, Germany's Xetra DAX by 7%, and Britain's FTSE 100 by 5.8%. In Japan, the Nikkei 225 hit a 19-year low on September 4th; it declined by 7.1% over the week.

American manufacturing failed to bounce back after July's sharp slowdown. The Institute of Supply Management's index remained at 50.5 in August, indicating minimal growth.

In the **euro area**, growth in both manufacturing and services also ground to a near standstill in August, according to surveys of purchasing managers. Retail sales fell by more than expected, declining by 0.9% in the year to June. Inflation rose from 1.9% in July to 2.1% in August, the highest annual rate since April and above the European Central Bank's ceiling of 2%.

Japan's economy grew at an annual rate of 1.9% in the second quarter, faster than expected. But revised figures showed that GDP had contracted by 0.1% in the first quarter rather than increasing by 5.7%, as previously estimated.

Data on more countries are available to subscribers on www.economist.com

Output, demand and jobs

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production latest	Retail sales (volume) latest		Unemployment % rate	
	1 qtr*	1 year	2002	2003		latest	Q2	latest	year ago
Australia	+ 2.4	+ 3.8 Q2	+ 4.0	+ 3.7	+ 4.3 Q1	+ 6.3	Q2	6.2 Jul	6.9
Austria	+ 0.3	- 0.6 Q1	+ 0.9	+ 2.4	+ 2.5 Jun	- 0.2	May	4.2 Jul	3.6
Belgium	+ 0.8	+ 0.3 Q2	+ 1.1	+ 2.7	- 4.1 Jun	- 4.2	Jun	12.0 Aug†	11.6
Britain	+ 2.4	+ 1.2 Q2	+ 1.7	+ 2.9	- 6.6 Jun	+ 4.5	Jul	5.1 Jun‡	5.0
Canada	+ 4.3	+ 3.2 Q2	+ 3.3	+ 3.4	+ 1.3 Jun	+ 4.3	May	7.6 Jul	7.0
Denmark	+ 4.4	+ 2.2 Q2	+ 1.6	+ 2.3	+ 4.2 Jun	+ 4.1	Jun	5.1 Jul	5.1
France	+ 2.0	+ 1.0 Q2	+ 1.3	+ 2.6	nil Jun	- 2.5	Jun	9.0 Jul††	8.7
Germany	+ 1.1	+ 0.1 Q2	+ 0.6	+ 2.2	- 2.3 Jun	- 1.7	Jul	9.6 Aug‡§	9.2
Italy	+ 0.9	+ 0.2 Q2	+ 0.8	+ 2.4	- 5.4 Jun	- 0.8	Jun	9.0 Apr	9.5
Japan	+ 1.9	- 0.9 Q2	- 0.5	+ 1.0	+ 3.3 Jul	- 3.5	Jun	5.4 Jul	5.0
Netherlands	+ 0.5	+ 0.1 Q2	+ 0.9	+ 2.4	- 3.0 Jun	- 2.1	May	2.4 Jul**	2.0
Spain	+ 1.8	+ 2.0 Q2	+ 2.0	+ 2.9	- 4.4 Jun	na		11.3 Jul	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.8	+ 2.7	- 1.3 Jun	+ 4.5	Jun	4.3 Jul†	4.2
Switzerland	+ 0.7	+ 0.2 Q1	+ 0.9	+ 2.2	- 8.8 Q1	- 3.0	Jun	2.7 Aug†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.5	+ 3.0	+ 0.2 Jul	+ 6.3	Jul	5.9 Jul	4.6
Euro area	+ 1.3	+ 0.3 Q1	+ 1.0	+ 2.4	- 1.2 Jun	- 0.9	Jun	8.3 Jul	8.0

*% change at an annual rate. †Not seasonally adjusted. ‡April-June; claimant count rate 3.1% in July. §EU harmonised rate 8.3% in July. **May-Jul. ††Revised series.

Prices and wages

% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2002	2003	latest	year ago	latest	year ago
Australia	+ 2.8 Q2	+ 6.0	+ 2.8	+ 2.5	- 1.1 Q2	+ 5.6	+ 3.7 Q2	+ 4.4
Austria	+ 1.6 Jul	+ 2.8	+ 1.7	+ 1.7	- 1.0 Jul	+ 1.9	+ 2.4 Jul	+ 2.8
Belgium	+ 1.3 Aug	+ 2.7	+ 1.7	+ 1.5	- 0.2 Jul	- 0.4	+ 2.6 Q2	+ 2.6
Britain	+ 1.5 Jul	+ 1.6	+ 1.9	+ 2.4	+ 0.3 Jul	- 0.1	+ 3.9 Jun	+ 4.7
Canada	+ 2.1 Jul	+ 2.6	+ 1.8	+ 2.2	- 0.3 Jul	+ 0.8	+ 3.0 Jun	+ 1.5
Denmark	+ 2.2 Jul	+ 2.4	+ 2.3	+ 2.0	- 0.9 Jul	+ 2.7	+ 4.0 Q1	+ 3.8
France	+ 1.6 Jul	+ 2.1	+ 1.8	+ 1.4	- 1.5 Jun	+ 2.3	+ 3.9 Q1	+ 4.3
Germany	+ 1.0 Aug	+ 2.6	+ 1.4	+ 1.2	- 0.8 Jun	+ 2.2	+ 2.5 Jun	+ 1.9
Italy	+ 2.3 Aug	+ 2.8	+ 2.3	+ 1.8	+ 0.1 Jul	+ 1.3	+ 2.2 Jul	+ 2.5
Japan	- 0.8 Jul	- 0.8	- 0.9	- 0.5	- 2.2 Jul	+ 0.7	- 5.6 Jul	+ 0.7
Netherlands	+ 3.5 Jul	+ 4.6	+ 3.6	+ 2.4	- 0.4 Jul	+ 2.4	+ 3.0 Jul	+ 5.1
Spain	+ 3.4 Jul	+ 3.9	+ 3.3	+ 2.6	+ 0.6 Jul	+ 2.0	+ 4.0 Q1	+ 3.4
Sweden	+ 2.2 Jul	+ 2.9	+ 2.3	+ 2.0	- 0.8 Jul	+ 2.1	+ 2.9 Jun	+ 2.8
Switzerland	+ 0.5 Aug	+ 1.1	+ 1.0	+ 1.2	- 1.6 Jul	+ 0.2	+ 2.5 2001	+ 1.3
United States	+ 1.5 Jul	+ 2.7	+ 1.6	+ 2.2	- 1.1 Jul	+ 1.4	+ 3.2 Jul	+ 4.1
Euro area	+ 2.1 Aug	+ 2.7	+ 2.1	+ 1.6	- 0.6 Jul	+ 2.1	+ 3.3 Q1	+ 2.8

Economic forecasts

Every month *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's forecasts, where different, are shown in brackets. Opinions about Japan are diverging: this month's range of projected growth rates is 2.7 percentage points for 2002 and 3.1 points for 2003. The panel expects a bigger contraction of Japanese GDP in 2002 and slower growth in 2003 than it did a month ago. It has also become less chirpy about the American economy, but still predicts that GDP will increase by 2.5% this year and by 3.0% in 2003. For the third successive month, the panel has become more pessimistic about the growth outlook in the euro area.

The Economist poll of forecasters, September averages (previous month's, if changed)

	Real GDP, % change				Consumer prices		Current account	
	Low/high range		average		% increase		% of GDP	
	2002	2003	2002	2003	2002	2003	2002	2003
Australia	3.4/4.6	3.2/4.3	4.0	3.7 (3.8)	2.8	2.5 (2.6)	-3.7(-3.4)	-3.8(-3.4)
Austria	0.5/1.3	1.8/2.8	0.9	2.4 (2.6)	1.7	1.7	-2.2(-1.9)	-1.9(-1.7)
Belgium	0.5/2.6	2.0/3.9	1.1 (1.3)	2.7 (2.9)	1.7	1.5 (1.6)	5.0 (4.8)	5.1 (4.9)
Britain	1.3/2.2	2.0/3.5	1.7	2.9	1.9	2.4	-2.1(-2.0)	-1.9
Canada	2.8/3.7	3.0/4.1	3.3	3.4 (3.5)	1.8 (1.7)	2.2	2.1 (2.4)	2.2 (2.5)
Denmark	1.2/2.1	1.9/2.5	1.6	2.3 (2.4)	2.3	2.0	1.9 (1.7)	1.8 (1.7)
France	1.1/1.8	2.0/3.2	1.3 (1.4)	2.6 (2.7)	1.8	1.4	1.7	1.6
Germany	0.4/1.0	1.5/3.0	0.6 (0.7)	2.2 (2.3)	1.4	1.2	1.2	1.0 (1.1)
Italy	0.5/1.4	1.5/3.0	0.8 (1.0)	2.4 (2.5)	2.3	1.8 (1.9)	-0.1	nil
Japan	-1.2/1.5	-0.1/3.0	-0.5 (-0.3)	1.0 (1.1)	-0.9 (-1.0)	-0.5	2.9 (2.8)	2.9 (2.8)
Netherlands	0.5/1.5	1.7/3.3	0.9 (1.0)	2.4 (2.5)	3.6	2.4 (2.3)	3.9 (4.0)	4.0 (4.2)
Spain	1.8/2.3	2.2/3.5	2.0 (2.1)	2.9 (3.0)	3.3	2.6 (2.7)	-2.1	-1.8
Sweden	1.4/2.0	2.2/3.1	1.8 (1.7)	2.7 (2.9)	2.3 (2.4)	2.0 (2.1)	3.2 (3.3)	3.2 (3.4)
Switzerland	0.5/2.0	1.3/3.7	0.9 (1.0)	2.2 (2.3)	1.0	1.2	10.0 (9.8)	10.2 (10.1)
United States	2.2/3.2	2.3/4.2	2.5 (2.7)	3.0 (3.4)	1.6	2.2	-4.5(-4.4)	-4.1(-4.7)
Euro area	0.7/1.4	1.9/3.0	1.0 (1.1)	2.4 (2.6)	2.1	1.6	0.5 (0.4)	0.5

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, Merrill Lynch, J.P. Morgan Chase, Morgan Stanley, Nordea, Decision Economics, BNP Paribas, Royal Bank of Canada, Schroder Salomon Smith Barney, Scotiabank, Shinsei Bank, UBS Warburg

Money and interest rates

	Money supply*			Interest rates % p.a. (Sep 4th 2002)					
	% change on year ago			3-mth money market		2-year	10-year gov't bonds		corporate bonds
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	
Australia	- 4.1	+ 9.4	Jul	4.86	4.78	4.82	5.48	5.79	6.69
Britain	+ 8.6	+ 5.7	Jul	3.94	4.70	3.72	4.47	5.01	5.64
Canada	+17.2	+ 7.2	Jul	2.97	3.81	3.19	4.88	5.50	6.96
Denmark	+ 6.2	+10.2	Jul	3.50	4.62	3.74	4.64	5.11	6.84
Japan	+30.6	+ 3.3	Jul	0.02	0.02	0.02	1.17	1.34	1.24
Sweden	+ 2.2	+ 4.2	Jun	4.18	4.31	4.41	4.94	5.23	4.93
Switzerland	+10.9	+ 5.8	Jul	0.73	3.18	0.77	2.77	3.33	3.98
United States	+ 5.2	+ 7.4	Jul	1.73	3.37	1.99	3.95	4.97	6.39
Euro area†	+ 7.6	+ 7.1	Jul	3.33	4.27	3.30	4.37	4.84	5.33

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.93%, Japan No. 241 1.20%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.001%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmssbörsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Stockmarkets

Market indices

	2002			% change on			
	Sep 4th			one week	record high	Dec 31st 2001	
		high	low			in local currency	in \$ terms
Australia (All Ordinaries)	3,047.5	3,440.0	2,937.8	- 1.4	-11.4	- 9.3	- 3.5
Austria (ATX)	1,124.5	1,357.2	1,113.5	+ 0.1	-35.3	- 1.4	+10.1
Belgium (Bel 20)	2,156.8	2,899.8	2,001.6	- 5.8	-41.4	-22.5	-13.5
Britain (FTSE 100)	4,026.9	5,323.8	3,777.1	- 5.8	-41.9	-22.8	-17.0
Canada (Toronto Composite)	6,517.7	7,958.1	6,161.1	- 0.9	-42.8	-15.2	-13.4
Denmark (KBX)	182.0	233.4	169.0	- 4.1	-39.7	-19.0	- 9.5
France (SBF 250)	2,148.1	3,081.9	2,067.7	- 6.6	-51.1	-27.9	-19.6
(CAC 40)	3,168.7	4,688.0	3,023.7	- 7.3	-54.2	-31.5	-23.5
Germany (Xetra DAX)	3,425.9	5,462.6	3,332.7	- 7.0	-57.5	-33.6	-25.9
Italy (BCI)	1,134.8	1,513.0	1,077.8	- 6.5	-48.0	-20.8	-11.6
Japan (Nikkei 225)	9,075.1	11,979.9	9,075.4	- 7.1	-76.7	-13.9	- 4.4
(Topix)	886.4	1,139.4	886.4	- 7.1	-69.3	-14.1	- 4.6
Netherlands (AEX)	349.7	531.2	318.5	- 7.3	-50.2	-31.0	-23.0
Spain (Madrid SE)	644.9	848.1	625.9	- 4.0	-43.7	-21.8	-12.7
Sweden (Affarsvarlden Gen)	147.6	236.8	143.1	- 4.6	-63.1	-36.2	-28.6
Switzerland (Swiss Market)	4,960.0	6,694.1	4,607.8	- 5.8	-41.0	-22.7	-12.9
United States (DJIA)	8,425.1	10,635.3	7,702.3	- 3.1	-28.1	-15.9	-15.9
(S&P 500)	893.4	1,172.5	797.7	- 2.7	-41.5	-22.2	-22.2
(Nasdaq Comp)	1,292.3	2,059.4	1,206.0	- 1.7	-74.4	-33.7	-33.7
Europe (FTSE Eurotop 300)*	905.5	1,279.7	862.3	- 6.0	-46.9	-28.2	-19.9
Euro area (FTSE Eblor 100)*	759.2	1,125.1	732.5	- 6.9	-51.0	-31.7	-23.8
World (MSCI)†	803.9	1,024.4	756.7	- 3.7	-44.5	na	-19.9
World bond market (Salomon)‡	502.6	504.2	430.3	+ 1.5	- 0.3	na	+14.3

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.

‡Salomon Smith Barney World Government Bond Index, total return, in \$ terms.

The Economist commodity price index

1995=100

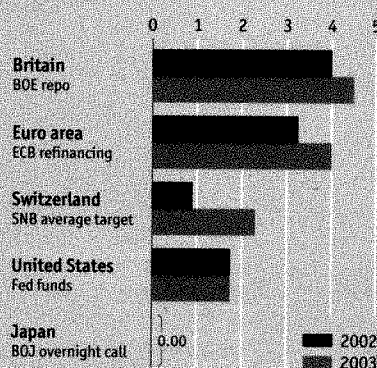
	Aug 27th	Sep 3rd*	% change on one month	% change on one year
Dollar index				
All items	73.2	73.8	+2.5	+9.1
Food	77.1	78.3	+3.6	+14.3
Industrials				
All	68.0	67.8	+0.8	+1.8
Nfa†	68.0	70.7	+0.2	+5.5
Metals	65.5	65.3	+1.2	-1.4
Sterling index				
All items	75.5	74.5	+0.8	+0.9
Euro index				
All items	98.3	97.4	-0.8	-2.5
Yen index				
All items	92.1	92.0	-0.7	+7.5
Gold				
\$ per oz	310.85	313.95	+2.7	+15.3
West Texas Intermediate				
\$ per barrel	28.83	27.77	+2.3	+3.0

* Provisional. † Non-food agricultural.

Interest-rate forecasts

Interest rates will stay on hold in America for the next 15 months, forecasts CSFB. It expects rates to rise in the euro area by three-quarters of a percentage point next year.

End of Q4, %



Source: Credit Suisse First Boston

Trade, exchange rates and budgets

	Trade balance*, \$bn		Current account				Exchange rate		Currency units					Budget balance % of GDP 2002†		
	latest 12 months		\$bn latest 12 mths		The Economist poll % of GDP, forecast 2002 2003		trade-weighted† Sep 4th year ago		per \$		per £	per euro	per ¥100			
									Sep 4th	year ago						
Australia	-	1.3 Jul	-	11.6 Q2	-	3.7	-	3.8	72.2	72.2	1.84	1.92	2.87	1.82	1.56	0.1
Austria	-	2.0 May	-	1.3 Jun	-	2.2	-	1.9	na	100.1	1.01	1.13	1.57	-	0.85	-0.3
Belgium	+	15.1 Jun	+	11.8 Mar§	+	5.0	+	5.1	na	98.7	1.01	1.13	1.57	-	0.85	nil
Britain	-	45.6 Jun	-	31.2 Q1	-	2.1	-	1.9	105.9	107.3	0.64	0.69	-	0.64	0.54	-0.8
Canada	+	34.0 Jun	+	12.1 Q2	+	2.1	+	2.2	75.8	77.0	1.56	1.56	2.45	1.55	1.32	1.0
Denmark	+	7.2 Jun	+	3.5 Jun	+	1.9	+	1.8	103.4	102.1	7.47	8.38	11.7	7.43	6.33	2.2
France	+	9.0 Jun	+	28.4 Jun	+	1.7	+	1.6	na	101.3	1.01	1.13	1.57	-	0.85	-2.0
Germany	+	100.6 Jun	+	27.2 Jun	+	1.2	+	1.0	na	98.2	1.01	1.13	1.57	-	0.85	-2.8
Italy	+	9.8 Jun	-	2.9 May	-	0.1	-	0.0	na	72.3	1.01	1.13	1.57	-	0.85	-1.4
Japan	+	80.6 Jun	+	107.0 Jun	+	2.9	+	2.9	136.6	140.3	118	120	185	117	-	-8.0
Netherlands	+	23.7 Jun	+	2.7 Q2	+	3.9	+	4.0	na	97.6	1.01	1.13	1.57	-	0.85	0.1
Spain	-	36.9 May	-	16.5 May	-	2.1	-	1.8	na	74.0	1.01	1.13	1.57	-	0.85	-0.3
Sweden	+	14.7 Jul	+	8.3 Jun	+	3.2	+	3.2	76.1	73.3	9.37	10.7	14.7	9.31	7.94	2.1
Switzerland	+	3.0 Jul	+	25.7 Q1	+	10.0	+	10.2	114.5	108.8	1.47	1.70	2.31	1.46	1.25	na
United States	-	435.5 Jun	-	398.1 Q1	-	4.5	-	4.1	112.5	118.6	-	-	1.56	0.99	0.85	-1.0
Euro area	+	79.2 Jun	+	24.8 Jun	+	0.5	+	0.5	82.0	78.0	1.01	1.13	1.57	-	0.85	-1.5

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast. §New series.

Overview

Argentina's economic woes intensified as consumer-price inflation accelerated to 36.7% in the year to August. Industrial production fell by 11.2% in the year to July.

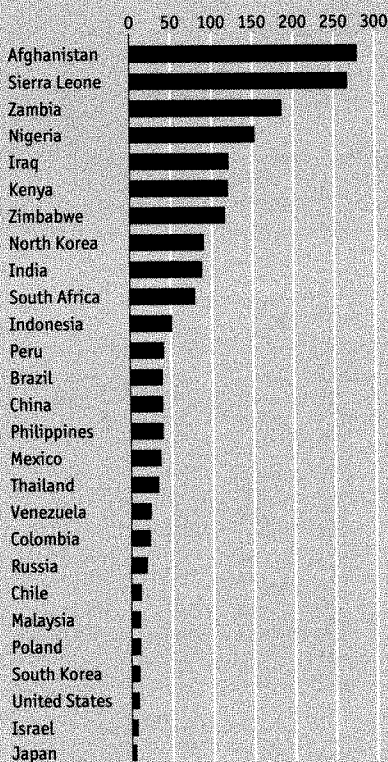
GDP in the **Philippines** grew by 4.5% in the year to the second quarter, the fastest rate for almost two years. **Hungary's** economy grew by 3.1% over the same period.

Industrial production rose by 9.6% in **Thailand** in the year to July.

Infant mortality, 2000

About 11m children below the age of five die every year around the world from preventable conditions such as malnutrition or illnesses caused by dirty air and water. Child-mortality rates are highest in Afghanistan and several countries in sub-Saharan Africa. In Zambia, Kenya and Zimbabwe, rates are now higher than in 1980. However, they have fallen by more than half in India, Indonesia and Peru over the past two decades. Two years ago, the United Nations agreed to a target to cut child-mortality rates by two-thirds by 2015. This objective may be helped by the agreement at the Johannesburg summit to achieve access to basic sanitation for more of the world's poor.

Under-5 mortality rate per 1,000



Source: World Bank

Economy

	% change on year ago				Latest 12 months, \$bn		Foreign reserves* \$bn, latest
	GDP	Industrial production	Consumer prices		Trade balance	Current account	
China	+ 8.0 Q2	+12.8 Jul	- 0.9 Jul		+28.3 Jul	+17.4 2001	241.9 May
Hong Kong	+ 0.5 Q2	-11.6 Q1	- 3.4 Jul		- 8.2 Jul	+14.1 Q1	112.3 Jul
India	+ 6.4 Q1	+ 4.0 Jun	+ 3.9 Jul		- 5.1 Jul	+ 1.4 Q1	56.5 Jul
Indonesia	+ 3.5 Q2	- 9.4 Q4	+10.6 Aug		+27.3 Jul	+ 8.4 Q3	29.5 Jul
Malaysia	+ 3.8 Q2	+ 4.9 Jun	+ 2.1 Jul		+13.4 Jul	+ 7.0 Q1	32.8 Jul
Philippines	+ 4.5 Q2	+ 5.9 Jun	+ 2.9 Aug		+ 2.6 Jun	+ 6.2 May	13.5 Jul
Singapore	+ 3.9 Q2	+17.8 Jul	- 0.4 Jul		+ 6.4 Jul	+17.5 Q2	80.3 Jul
South Korea	+ 6.3 Q2	+ 8.9 Jul	+ 2.4 Aug		+ 9.8 Aug	+ 5.3 Jul	115.4 Jul
Taiwan	+ 3.0 Q2	+11.4 Jul	+ 0.4 Jul		+18.6 Jul	+24.8 Q2	155.3 Jul
Thailand	+ 3.9 Q1	+ 9.6 Jul	+ 0.3 Aug		+ 3.8 Jul	+ 6.5 Jul	37.0 Jul
Argentina	-16.3 Q1	-11.2 Jul	+36.7 Aug		+12.6 Jun	nil Q1	9.0 Jul
Brazil	+ 1.0 Q2	+ 0.7 Jun	+ 7.5 Jul		+ 7.4 Aug	-16.7 Jul	39.1 Jul
Chile	+ 1.7 Q2	+ 8.6 Jul	+ 2.1 Aug		+ 2.7 Jul	- 0.6 Q2	15.0 Jul
Colombia	+ 0.5 Q1	- 1.2 Jun	+ 6.2 Jul		+ 0.5 Jun	- 1.4 Q1	10.6 Jul
Mexico	+ 2.1 Q2	- 0.7 Jun	+ 5.5 Jul		- 9.1 Jul	-16.3 Q2	46.1 Jul
Peru	+ 3.6 Jun	+ 2.8 May	nil Jul		+ 0.2 Jun	- 1.0 Q2	9.2 Jul
Venezuela	- 9.9 Q2	-17.1 Jun	+22.0 Jul		+ 8.0 Q1	+ 1.9 Q2	7.6 Jun
Egypt	+ 4.9 2001†	+ 7.8 2001†	+ 2.7 Jun		- 8.2 Apr	- 0.1 Q1	12.7 Apr
Israel	- 1.7 Q2	+ 1.6 Jun	+ 6.9 Jul		- 6.3 Jul	- 2.3 Q1	24.5 Aug
South Africa	+ 2.2 Q2	- 0.1 Jun	+10.6 Jul		+ 3.1 Jul	- 0.1 Q1	6.0 Jul
Turkey	+ 2.3 Q1	+ 6.6 Jun	+40.2 Aug		-10.3 Jun	- 2.0 May	23.2 Jul
Czech Republic	+ 2.5 Q2	+ 1.3 Jun	+ 0.6 Jul		- 2.5 Jun	+ 2.3 Q2	21.4 Jul
Hungary	+ 3.1 Q2	+ 4.1 Jun	+ 4.6 Jul		- 2.4 Jul	- 2.1 Jul	10.3 Jul
Poland	+ 0.5 Q1	+ 6.0 Jul	+ 1.3 Jul		-10.4 Jul	- 6.4 Jul	27.1 Jul
Russia	+ 3.7 Q1	+ 7.8 Jul	+15.2 Aug		+42.4 Jun	+28.3 Q2	39.6 Jul

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Financial markets

	Currency units		Interest rates	Stockmarkets	% change on		
	per \$	per £			one week	in local currency	in \$ terms
	Sep 4th	year ago	Sep 4th	Sep 4th			
China	8.28	8.28	13.0	na	1,736.8	-0.8	+ 1.4
Hong Kong	7.80	7.80	12.2	1.73	9,820.3	-3.1	- 13.8
India	48.4	47.2	75.8	5.76	3,173.4	+2.4	- 2.7
Indonesia	8,870	9,055	13,878	14.83	420.4	-5.1	+ 7.2
Malaysia	3.80	3.80	5.95	3.20	707.9	-2.3	+ 1.7
Philippines	51.8	51.2	81.1	7.00	1,114.0	+0.4	- 4.6
Singapore	1.75	1.75	2.73	0.88	1,457.5	-3.2	- 10.2
South Korea	1,192	1,277	1,865	4.80	723.1	-0.1	+ 4.2
Taiwan	34.2	34.6	53.5	2.10	4,534.2	-5.3	- 18.3
Thailand	42.2	44.3	66.0	2.00	351.9	-3.6	+ 15.8
Argentina	3.64	1.00	5.69	68.70	373.7	-0.9	+ 26.5
Brazil	3.14	2.56	4.92	17.82	9,996.9	-3.7	- 26.4
Chile	717	664	1,123	2.40	4,905.2	-0.7	- 9.1
Colombia	2,703	2,315	4,228	8.00	1,191.3	+0.1	+ 11.2
Mexico	10.02	9.25	15.7	6.90	6,114.4	-0.0	- 4.0
Peru	3.63	3.48	5.69	3.25	1,185.8	-0.4	+ 0.9
Venezuela	1,432	740	2,240	30.08	6,835.4	-1.3	+ 4.0
Egypt	4.60	4.26	7.20	7.15	5,230.9	-0.6	- 0.8
Israel	4.73	4.29	7.40	6.40	357.3	-2.9	- 20.0
South Africa	10.7	8.50	16.7	12.45	9,498.0	-2.2	- 9.0
Turkey	1,628,500	1,413,500	2,547,951	42.00	9,469.8	+0.8	- 31.3
Czech Republic	30.5	38.4	47.8	3.04	439.7	-3.2	+ 11.4
Hungary	247	283	386	9.76	7,336.8	-4.7	+ 2.9
Poland	4.13	4.24	6.46	8.30	12,857.1	-4.6	- 7.7
Russia	31.6	29.5	49.5	21.00	334.3†	-3.8	+ 33.4
EMF (MSCI)*	1.00	1.00	1.56	na	291.3	-2.2	na
EMBI+†	1.00	1.00	1.56	na	206.8	+0.4	na

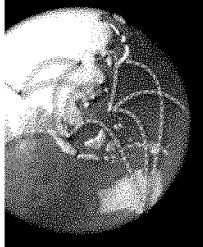
*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In \$ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; UBS Warburg; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; Russian Economic Trends.

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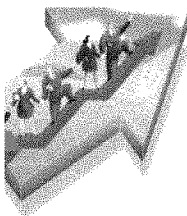
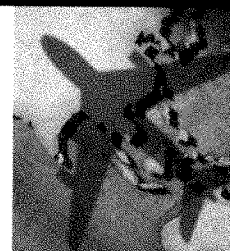
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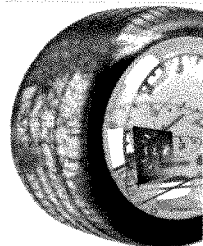
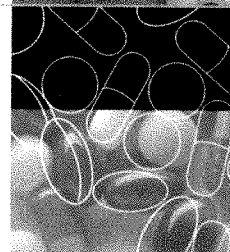
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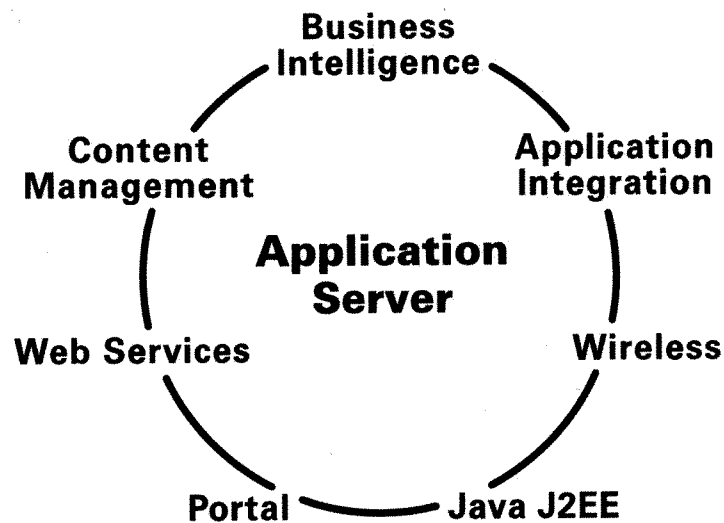
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Confronting Iraq



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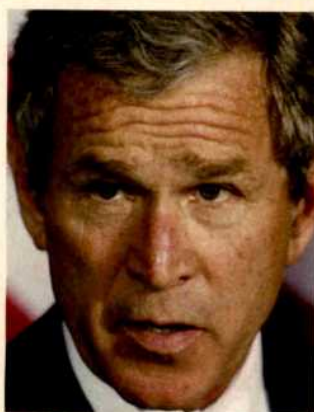
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On the cover

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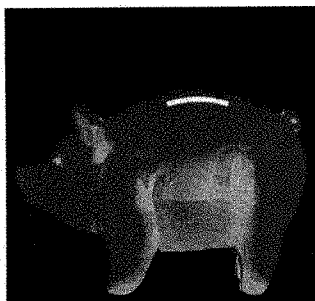
Special report Oil If America goes to war against Iraq, vast reserves of oil will be added to the world market—eventually. Would it be the end of OPEC? Pages 22-24



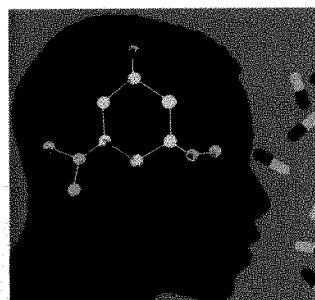
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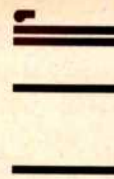
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Politics



Commemorations took place around the world to mark the first anniversary of **September 11th**. At Ground Zero in New York city there was a minute's silence at 8.46am, the moment last year when the first aircraft hit the World Trade Centre. The anniversary was accompanied by warnings of possible further terrorist attacks.

Pressure on **Iraq** increased. George Bush met Tony Blair to discuss Saddam Hussein, before going to the United Nations to present his case against the Iraqi dictator. Meanwhile the Pentagon sent 600 members of its Central Command headquarters to the Gulf.

Janet Reno seemed to have narrowly lost the Democratic gubernatorial primary in **Florida**, though the contest was once again marred by problems with voting machines. A local businessman, Bill McBride, will now run against the Republican incumbent, Jeb Bush.

In **New Hampshire**, Bob Smith became the first sitting senator to be ejected in a primary since 1992, losing to John Sununu, a young Republican congressman and son of the governor of the same name.

Not content with passing America's most generous ever **farm bill** a mere four months ago, the Senate voted an additional \$6 billion in aid to farmers. The new bill will be a test of Mr Bush's determination to rein in spending.

Lacking confidence

In a blow to **Yasser Arafat's** authority, his cabinet, which he had reformed in June under American pressure, resigned to avoid a parliamentary motion of no confidence. Mr Arafat had earlier announced that elections would be held on January 20th, without, or so he hoped, the disabling obstacles of Israeli closures and curfews.

Mr Arafat's **Fatah movement** issued a draft declaration that called on all Palestinian organisations to stop attacking Israeli civilians. But members continued to argue over the exact wording.

Ariel Sharon, Israel's prime minister, gave warning that a Lebanese plan to pump water from the **Wazzani river**, a source of the Hasbani river which is shared by the two countries, would be something "Israel could not abide".

An Israeli army inquiry decided that soldiers who had killed 13 **Palestinian civilians** in three recent incidents had followed correct procedure. An Arab-Israeli accused of assisting a militant Palestinian organisation was stripped of his citizenship.

Al-Jazeera, an Arab satellite-television station, broadcast a videotape said to feature **Osama bin Laden's** voice naming all 19 of the "men who changed the course of history", in other words the terrorists who attacked America last September.



Malawi's parliament, which in July rejected a bill to abolish term limits for the president, is to debate the issue again. President Bakili Muluzi must stand down in 2004 un-

less the constitution is amended. His government will re-propose the amendment next month.

In **South Africa**, the constitutional court ruled that gay couples may adopt children. Unlike most other African countries, where homosexuality is abhorred or illegal, South Africa's constitution forbids discrimination.

Zimbabwe's opposition party said that half of its 1,397 candidates for local elections, scheduled for later this month, had been prevented from registering their candidacy, as ruling-party thugs had threatened to kill them.

Going for gold

In **Brazil**, opinion polls showed support for Luiz Inacio Lula da Silva rising to around 40%, giving him a small chance of outright victory in the election on October 6th. Jose Serra, the government candidate, consolidated his grip on second place with around 20%, making a run-off ballot between the two men probable.

Colombia's new government, invoking the state of "internal commotion" decreed last month, gave security forces greater powers of arrest and restriction on freedom of movement. Human-rights groups protested.

Mexico announced its withdrawal from the Rio Pact, a mutual-defence treaty for the Americas dating from the days of the cold war.

Opposition stirred to the proposed **Free-Trade Area of the Americas**. Brazil's Catholic bishops organised a "plebiscite" against it. Venezuela's government promised a referendum on it next year.

Guns and ballots

Suspected Islamic militants killed 18 people in two separate attacks in Indian-administered **Kashmir**. Among the dead was Kashmir's law minister, Mushtaq Lone. The attacks are thought to be

designed to disrupt voting in the state election, due to start on September 16th.



At least 100 people were killed when a train **derailed** travelling from Calcutta to Delhi. Over 250 people were injured.

Pakistani police killed two gunmen and arrested five others after a three-hour shootout in the southern city of Karachi. The men are suspected of being members of al-Qaeda.

Too close to call

All **Germany's** main opinion pollsters put the two main parties competing in the general election on September 22nd neck-and-neck, with the ruling Social Democrats and the conservative Christian Democrats (together with their Bavarian allies in the Christian Social Union) each having about 39%.

Austria's ruling coalition of mainstream and populist conservatives collapsed after a row within the populist camp. The chancellor, Wolfgang Schüssel, who heads the mainstreamers, said a general election would take place in early December at the latest.

Vladimir Putin, **Russia's** president, said that his country had a "right to self-defence" if neighbouring Georgia failed to expel rebel Chechens living there, implying that Russian forces might cross the border to attack them.

Though not disavowing its traditional neutrality, **Switzerland** joined the UN as its 190th member.

Flash floods in the south of **France** left 21 people dead and several unaccounted for.

Business

A cash crisis at **British Energy** sent shares in Britain's privatised nuclear-energy generator into meltdown and reduced the company's credit rating to junk status. The British government reacted by offering £410m (\$635m) in loan guarantees to help the ailing power generator stave off bankruptcy while it attempts to restructure its finances.

British Airways succumbed to competition from low-cost carriers and the post-September 11th troubles of the airline industry. It fell out of the FTSE 100 share index of Britain's biggest companies, for the first time since the airline was privatised in 1987.

Star wars

A space race broke out for **Eutelsat**, the world's fourth-largest satellite company. **Pan-AmSat** and **Intelsat**, respectively numbers two and three in the business, are after their European rival, although only Intelsat has made a formal bid—of around \$4 billion. The victor would rival SES Global of Luxembourg, the world leader in a business dogged by overcapacity.

Jürgen Dormann took over as chief executive of **ABB** on the departure of Jörgen Centerman after 18 months in charge at the troubled Swiss-Swedish engineering group. Mr Dormann, ABB's chairman, said that his strategy of selling assets to concentrate on core businesses could take time to show results, but he also tried to ease fears about debt and the extent of any exposure to asbestos.

A heavily discounted rights issue that will raise £768m (\$1.2 billion) for **Legal & General**, a British life insurer, hit shares in other big rivals. Cash to finance growth, claimed L&G, not to plug a hole in the balance sheet. A struggling rival insurer, **Royal & Sun Alliance**, got rid of its chief executive, probably presaging a cash call on investors.

Cutting off MobilCom?

MobilCom suffered a fall of over 50% in its share price in the run-up to a board meeting at France Telecom, which owns 28.5% of the German mobile-phone company. Investors fear that the part-privatised French company will force MobilCom into bankruptcy. France Telecom was also expected to announce a rights issue of €15 billion (\$15 billion), and to shed its chairman, Michel Bon.

The European Commission gave preliminary assent to a deal that would allow Germany's **T-Mobile** and Britain's **mmO2** to share the cost of building third-generation mobile-phone networks in Britain and Germany. Many more such deals may be in the works as mobile-phone companies seek to recoup some of the \$100 billion-plus that they paid for 3G licences during the telecoms boom.

Crown Prince

Citigroup replaced Michael Carpenter as head of Salomon Smith Barney, its investment-banking arm. Charles Prince, a lawyer, took over. Citigroup also announced a new committee to beef up its corporate governance. Regulators investigating Salomon for its prac-

tice of allocating shares in initial public offerings to favoured clients and those looking into Citigroup's role in the WorldCom and Enron scandals may feel more action is needed.

An American congressional committee asked the Department of Justice to investigate whether **Martha Stewart** had obstructed justice by lying to prosecutors over allegations of insider dealing. Shares in the lifestyle doyenne's company rebounded handsomely after the news that she had avoided formal charges—for the moment.

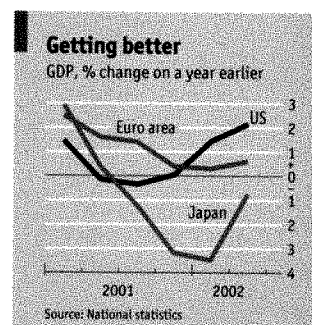
WorldCom is to replace its chief executive, John Sigmund. The company's board evidently concluded that the scandal-hit telecoms giant, which went into Chapter 11 bankruptcy in July, needs different managers from those who presided over its fall if it is ever to recover.

Markets remember

World stockmarkets paused in trading for a moment's silence to commemorate victims on the anniversary of the September 11th terrorist attacks. Wall Street trading began late, after ceremonies to remember the dead.

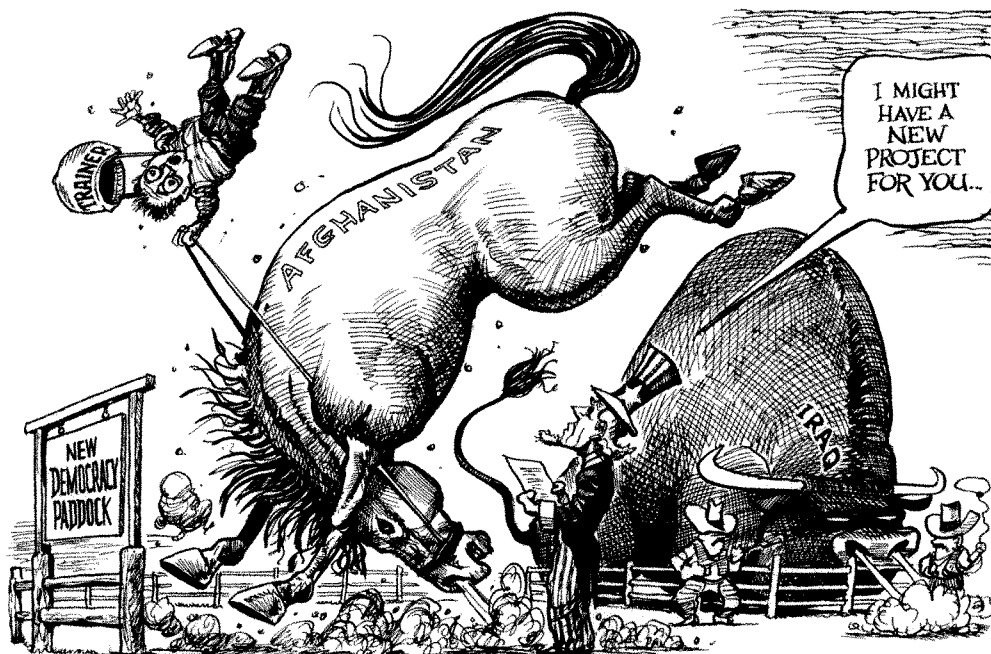
After a period of quiet, fresh rumours circulated of plans for a **24-hour stock exchange**. Hong Kong Exchanges & Clearing is in talks with the National Association of Securities Dealers to acquire a stake in the American Stock Exchange, America's third-largest exchange.

Going for growth



America's economy seems to be recovering faster than the world's other big economies despite the effects of the September 11th 2001 attacks. Euro-area GDP grew by just 0.6% in the second quarter over a year earlier. Japan's growth for the quarter was revised up slightly, growing by 0.6% over the previous quarter, thus ending a prolonged recession.

Other economic data and news can be found on pages 88-90



Seven out of ten expats should be making more money.

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Confronting Iraq

Saddam Hussein must be dealt with—by the United Nations if possible, without it if need be



TO HEAR his many critics tell it, George Bush had serious charges to answer this week before the United Nations court of international opinion. The leader of the free world stands accused of threatening to disrupt international law and order.

America's insistence that Iraq be stripped of its illicit weapons of mass destruction, as a matter of urgency, by force if necessary, is anyway surely a ruse, since Mr Bush has publicly admitted his aim is to topple the regime of Saddam Hussein. Although America has called on others to join it, Mr Bush has said he will go it alone if necessary. Such rampant unilateralism undermines the very authority of the United Nations.

The charges are preposterous. Yet Mr Bush had some explaining to do. In a democracy, any leader contemplating going to war has a duty to explain—in Mr Bush's case to Congress and the American people, but also to the wider world—why this needs to be done. His speech to the UN General Assembly on September 12th came too late for *The Economist* to gauge its impact. But whether the world stands with him in dealing with the menace Iraq poses, as he has asked it to, or against him, it is not Mr Bush who needs hauling into the dock, but Iraq's dangerous regime, and those members of the UN Security Council which for years have helped Iraq wriggle out of the disarmament obligations the council itself imposed.

Ends and means

"Not without United Nations approval" is the near-universal chant that has greeted Mr Bush's insistence that doing nothing about Iraq's illicit weapons is no longer an option—as if the Security Council were the moral conscience of the world. Would that it were. It is instead a collection of powerful states, all pursuing their own interests with what one can only hope is a sense of wider responsibility. There was nothing high-minded, for example, about Russia's refusal to countenance military action to halt Slobodan Milosevic's ethnic cleansing of Kosovo. It backed the butcher of the Balkans to the bitter end. Some still claim that NATO's intervention there was illegal, since it lacked explicit UN endorsement. Yet 19 of the world's strongest democracies were surely right to act where the UN, divided, could not.

The case of Iraq is different, admittedly. Saddam Hussein has killed far more of his own people and his neighbours than Mr Milosevic ever did; and he has sent his armies and his rockets well beyond Iraq's borders. The Security Council, at first letting principle triumph over pusillanimity, repeatedly declared him in open breach of his disarmament obligations. What it failed to do was rectify that situation. When it came to the crunch—authorising force to back up the inspectors' right to search out and destroy Iraq's nuclear, chemical and biological stocks—first Russia and China backed off, keen to close all weapons accounts, see UN sanctions lifted and return to oil-business-as-usual. Then France did the same, leaving America and Britain to attempt to hold the line.

The result has been much worse than stalemate: as a report by the International Institute for Strategic Studies points out, Mr Hussein has hung on to his still-hidden arsenal and has had four years free of inspections to restore and conceal as much as he could of what the inspectors had earlier destroyed (see page 39). To those who, when told that Iraq is a mortal threat to the peace of the world, say "prove it", the only sane reply is: what more proof could anyone need?

If it was right to act in Kosovo where the Security Council was stymied, it is surely right to act in Iraq where the council has failed, with potentially disastrous consequences, to deal with what it has accepted itself is an even more potent threat. Then ask yourself, who is undermining the authority of the UN and its Security Council—those who seek to uphold its repeated resolutions on the nuclear, chemical and biological frisking of Iraq, or those who stand in the way?

Credible threats

Yet while it may sometimes, regrettably, be necessary to act without UN approval, isn't America guilty at best of poor judgment, at worst of hypocrisy, in calling not just for inspectors to return to disarm Iraq but for Mr Hussein to be turfed out of power? Won't he be even more tempted to use his horrific weapons rather than see his regime destroyed?

The fact is, it has taken the credible threat of massive force to get Iraq's—and others'—attention. Without it, Mr Hussein would not even be hinting at new inspections (someday, with strings attached). Russia would not now be forced to contemplate how closely to move alongside Mr Bush in order to protect its business dealings in a post-Saddam Iraq. France's president would not this week be reversing himself, to propose a tough new Security Council resolution demanding that Iraq admit inspectors within three weeks, or else (though the "or else" still has no force to it).

If Mr Hussein's only concern were to stay in power, he could have done so by handing over his banned weapons and had sanctions lifted. Instead he has treated inspections as a continuation of the Gulf war by other means. That suggests he has more dangerous plans. It is plausible to conclude that Iraq will not give up its weapons of mass destruction unless he goes. And if he were to surprise the world, and hand them over after all? Then even Mr Bush might conclude that the threat he poses had been suitably deflated.

It is the Security Council's failure to rid Iraq of its weapons of mass destruction, not a gun-slinger's determination to look for trouble, that prompts Mr Bush to insist that America, with others where possible, must finish the job. Yet it is not too late for Russia, China and others who say they want him to work with the UN rather than around it to come up with a properly effective plan for dealing promptly with the threat Iraq's weapons pose. All they have lacked is the will. And for his part, Mr Bush knows that the more international support he can muster, the better, not just to contain and disarm Iraq, but to set the place on its feet properly again once the disarming is done. Why else bother to take his case to the UN at all? But, with or without the UN, disarmed Iraq must be. ■

Afghanistan

Securing the peace

The international security force should be extended beyond Kabul



NOT for the first time, some of the rhetoric on the lips of Afghanistan's would-be protectors and rebuilders sounds a bit surreal to ordinary people—both inside and outside that country—who are concerned about its future. As interna-

tional attention has drifted to a possible next confrontation, with Iraq, officials still trying to rescue Afghanistan from the rubble of 20 years of civil war have found it increasingly hard to squeeze the cash out of some of the governments that just a few months ago had made generous-sounding promises of assistance. Now the Bush administration has reversed itself and declared its active support for the extension of the multinational peacekeeping mission—known as the International Security Assistance Force (ISAF)—from Kabul to other cities.

A commendable idea, people in Kabul might agree—but can the Americans and their allies really mean this? As of now, it is not even certain whether ISAF will remain in the country at all beyond the end of the year. A new UN resolution will be needed, and another country will have to be induced to lead the force when Turkey's mandate expires in December.

Given the steady stream of reports of recent shootings and bombings, the worry of governments, taxpayers and soldiers' families involved in Afghan peacekeeping about extending ISAF will be different. Might America and its friends be about to get bogged down in Afghanistan in a new version of the tragedy which occurred in Somalia in 1992-93, where a multinational operation which started with high ideals ended in an obscure but all too bloody feud?

In fact, the extension of ISAF is more than a good idea. It is

probably essential if Afghanistan is to avoid sliding back into the morass of past rivalries. The force has done an excellent job in Kabul, showing how a discreet military presence, patrolling the streets and gathering intelligence, can have a subtle but powerful effect in shoring up a fragile peace. ISAF was not able to avert last week's car bomb; but people in the Afghan capital have generally felt safer—and less likely to be caught up in skirmishing between warlords—than their compatriots in other cities. In places like Mazar-i-Sharif or Herat, the situation is certainly tense and difficult, but not hopeless; a well-planned deployment by ISAF could make all the difference.

Lessons have been learned from other peacekeeping operations, from the Balkans to the Horn of Africa, successes and failures alike. To succeed, such missions need the broad agreement of all local parties who wield a significant amount of force. Afghanistan (or at any rate those places, including all the cities, where the Taliban have been smashed) meets that test. Since the Bonn agreement last December, all the non-Taliban forces have been committed to rebuilding a peaceful, united country with western help.

Peacekeepers must also have enough force to back them up if attacked, but must be capable of reaching out to ordinary people, by dealing with community leaders and assisting in humanitarian work. ISAF has done that in Kabul, and it can do so elsewhere—so long as the ground is prepared by careful intelligence work and local diplomacy. Tension still simmers in the north between leaders of the Uzbeks and the Tajiks—the two ethnic groups which made up the northern alliance. An international force could help keep a lid on violence there.

As everyone now accepts, the cost of allowing Afghanistan to become a "failed state" has been tragically high. That makes the cost of extending ISAF surely worth paying. ■

Israel

Crushing Palestine is no answer

Israel's prime minister and chief of staff seem set on a total victory against occupied Palestine



AN END to the Israeli-Palestinian tragedy stretches out of sight, but every so often there comes a chance which, if snatched, might alleviate today's pain. Each time, this chance is muffed. The hope of a ceasefire, or an opening to a less

savage situation, is blown away, usually by some brutal deed.

A lull in the violence, encouraging talk of some kind of interim agreement, is smashed, either by a terrorist bomb or by Israel assassinating a militant or raiding the heart of Palestinian territory. Terrorists calculate that they have an interest in maintaining a scary haze of violence. But what about Israel? Some of its leaders, it seems, also doubt that a peaceful respite

would be in their best interests.

The latest attempt to break out of the cycle of violence and oppression was the "Bethlehem, Gaza first" plan thought up by Binyamin Ben-Eliezer, Israel's defence minister. In return for the Palestinians cutting down on violence, the Israeli army would relax its restrictions, first in the two named areas, and then elsewhere. The plan has worked in Bethlehem but has yet to be tried in Gaza, let alone anywhere else.

In reply to continued low-level Palestinian violence in Gaza, Israel has twice within two recent days driven its tanks deep into the territory. The unfortunate Mr Ben-Eliezer is trapped, and undermined, by a commanding combination from above and below. Both his prime minister, Ariel Sharon, and his new chief of staff, Lieut-General Moshe Yaalon, have made it plain that they have no time for his plan. Similarly, this ►►

week's call, by Yasser Arafat and his Fatah movement, for an end to killing civilians, received a swift brush-off.

General Yaalon has explained, lucidly and at length, the philosophy behind his determination to keep hammering the Palestinians until he gets their unconditional surrender. He is not a political right-winger, as his predecessor was, yet he believes the Palestinians pose a "cancerous" threat to Israel's very existence: they are not, in his view, fighting to end the occupation but to liquidate Israel itself. Israel, therefore, must go for total victory. The Palestinians must be beaten in an unambiguous way that sears into their obstinate minds that they must never try anything against Israel again.

The army has been given its head: its recent killing of 13 Palestinian civilians in three incidents got a quick military white-wash. Worse, the chief of staff opposes any pre-victory deal from which the Palestinians might scent Israeli weakness. Israel's unilateral withdrawal from Lebanon, he argues, was a bad mistake that sent the wrong message to Israel's enemies.

Mr Sharon, who defends General Yaalon as "a level-headed person", seems to share his views. He insists that Israel should concede nothing in the face of terrorism. That sounds reasonable, but all Palestinians, and some Israelis too, have

come to believe that one of his main motives in giving the go-ahead to apparently poorly-timed pre-emptive action is to pre-empt a prolonged ceasefire. This, he fears, might evolve into a situation where he was under pressure to make territorial concessions in return for peace. "Oslo doesn't exist, Camp David doesn't exist, neither does Taba," said Mr Sharon last week, dismissing the agreements, or attempts to get agreement, that were based on the principle of land for peace.

Without hope

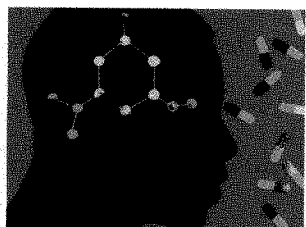
Casting out the land-for-peace equation casts out Palestinian hope. General Yaalon's blanket charge that the Palestinians aim to eliminate Israel distorts the goal of a people living under occupation, most of whom are trying only to win back their land. And loss of hope breeds supporters for the terrorists. Last week, a nervous Israeli public saw a car carrying half a tonne of explosives stopped at a road block. This week, Palestinians were arrested for allegedly trying to poison food.

Such acts are despicable, and Israel has to guard itself against them. But the refusal to deal at all, implicit in General Yaalon's perception of the Palestinians as an enemy only to be flattened, leads directly to an open-ended war of attrition. ■

Intellectual property

Imitation v inspiration

How poor countries can avoid the wrongs of intellectual-property rights



"THE public will learn that patents are artificial stimuli to improvident exertions; that they cheat people by promising what they cannot perform; that they rarely give security to really good inventions, and elevate into importance a

number of trifles...no possible good can ever come of a Patent Law, however admirably it may be framed."

Hardly an argument you might expect *The Economist* to endorse. And yet this passage appeared in our pages in 1851. In the mid-19th century, *The Economist* believed that patents hindered rather than helped growth, by restricting the free use of one man's ideas by another. By all means let inventors be rewarded, we argued, but by trying their luck in the open market. Patents, like protection, were an enemy of free trade.

How times change. In today's "knowledge economy", patents seem to be central to western notions of prosperity and international trade. Signing on to the global agreement on intellectual property, called TRIPS, is now part and parcel of membership of the World Trade Organisation.

Most of the world's people live in countries which either do not have, or do not enforce, intellectual-property rights. Not for much longer, however: TRIPS requires even the least-developed countries to have some minimum protection in place by 2006. Whether this is good for the poor is hotly debated. America, which has the most extensive and expensive national-patenting system in the world, preaches that patents help to foster growth in poor places, since they stimulate domestic innovation, boost foreign investment and improve access to new technologies.

Nonsense, retort many poor-country governments. Western-style intellectual-property protection brings many costs and few benefits. Patent systems are expensive to implement, draining scarce money and trained manpower from other more pressing concerns. Patents hurt, rather than help, domestic industries, which are often based more on copying than on innovating. And in the process, western patent rules prevent poor people from getting life-saving drugs, interfere with age-old farming practices and allow foreign "pirates" to raid local biodiversity or traditional handicrafts, without getting permission or paying compensation.

Into this fray now steps a study by an international commission set up by the British government to examine how intellectual-property rights can help or hinder developing countries (see page 67). It questions the doctrine that patents are good for the poor. There is little evidence to show that truly downtrodden places which introduce robust intellectual-property protection reap any of the much-touted benefits. Certainly, patents matter greatly to some industries, such as pharmaceuticals. But putting in a rigorous patent system will not make Angola a hotspot of biotechnology innovation any time soon; a licence to drive is little use without a car.

For richer, for poorer

Rich countries should remember this when they seek to impose their intellectual-property regime on the rest of the world. It is entirely reasonable for the world's poorest countries to argue that they need until 2016, at least, to adopt and enforce patents on pharmaceuticals. This stay of execution should, indeed, be extended to all forms of intellectual property. Poor countries should also be wary of any provisions in trade deals that try to impose stronger intellectual-property

standards than TRIPS requires, or of any moves towards universal, one-size-fits-all patents in such controversial areas as biotechnology. Rich countries should accept that considerations of how intellectual-property rights affect poor countries are not just a concern of overseas-aid agencies, but play a part in broader trade and economic relations too.

That is not to reject intellectual-property rights in the poor world altogether. Applied in the right way and at the right moment in development, they offer opportunities not threats to poor people. Some developing countries, such as India and China, whose industrial-scale copying of other people's products alarms Western businesses, are sufficiently advanced to

support the sort of innovation that would benefit from patents. They should bring their systems up to scratch, for the sake of their own industry. Even the poorest countries can profit from well-designed intellectual-property protection. Senegal, for example, has thousands of musicians who would benefit from copyright enforcement.

Carefully worked-out policies for protecting intellectual property will not solve developing countries' bigger problems, such as inadequate health care, lousy schools and sheer poverty. But if they are adapted to fit individual countries' circumstances, they can play a helpful role in nurturing the domestic industries that lasting growth requires. ■

Nuclear power

A dark day in Britain?

No: the collapse of British Energy is a triumph for energy liberalisation



AS BRITAIN'S privatised nuclear energy generator teeters on the edge of bankruptcy, two ideas are gaining currency. One is that British Energy's collapse, coming as it does on the heels of the recent power crisis in California and the collapse of

Enron, proves that electricity deregulation is a failure. The other is that the nuclear industry is unsafe in private hands. Both are wrong.

Britain used to have a "pool" arrangement for electricity trading, which allowed generators (including British Energy) to manipulate prices to boost their profits. That system was recently binned. One consequence is that electricity wholesale prices have fallen by around 40% since 1998, and much of that saving has been passed on to businesses and householders. A second consequence is that it has become clear that there is too much electricity-generating capacity. And a third consequence is that British Energy, which has higher costs than its competitors, can no longer compete. On September 5th, the company announced that it was about to go bust; trading in its shares was suspended; and four days later the government announced a £410m (\$635m) rescue package to keep it temporarily afloat.

The idea that British Energy's problems are an indictment of liberalisation is an odd one. A market that used to be rigged by producers to the detriment of consumers is now genuinely competitive. Today's victims are the high-cost generators, not buyers of power. The sharp drop in prices and the excess generating capacity prove that the industry was operating inefficiently, and that consumers were paying too much.

Liberalisation has exposed the true costs of nuclear power, and of the political burdens which the British government has chosen to impose on British Energy (see page 47). In that sense also, the company's financial problems are a measure of the success, not the failure, of the new trading system. Its openness makes economic inefficiency and political fudge harder to hide.

So what should the government do now? Those who want it to spend more taxpayers' money keeping the company afloat argue that there are two grounds for doing so: nuclear

safety and security of supply.

The government certainly needs to ensure that nuclear fuel and waste are handled safely. British Energy is not a widget maker. However, it is perfectly possible for officials to keep fissile materials from Osama bin Laden even if the firm goes bust. The second, and more challenging, test is to keep the lights on. California's blackouts are a poor argument for bailing out British Energy. California never properly liberalised its market—while wholesale prices were allowed to fluctuate, for instance, retail prices were capped. Britain's liberalisation has been far better managed.

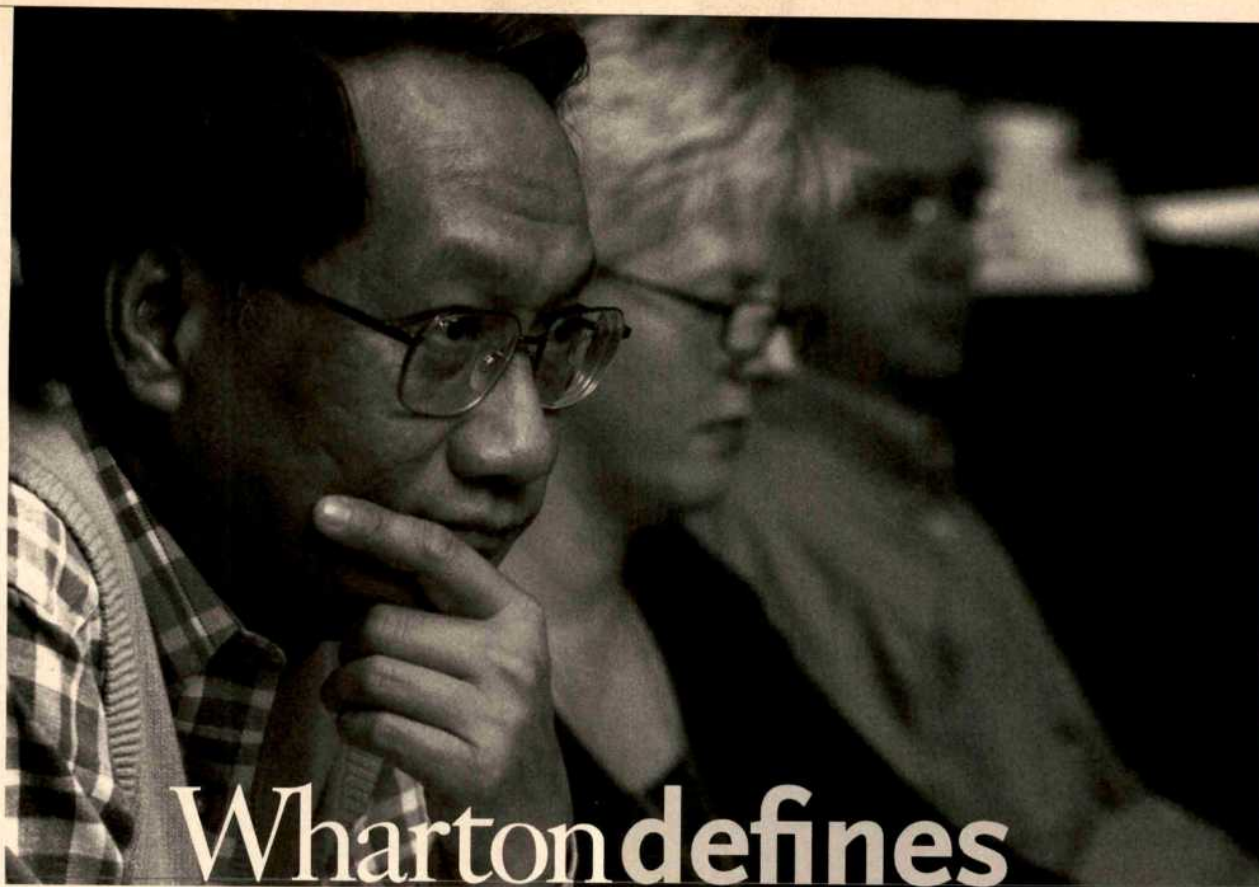
If British Energy went under, would the lights go out? No. Were the company to be declared insolvent and go into receivership, any sensible receiver would keep the plants running. And any new owner—if one could be found to take over this dismal prospect for a pittance—would have every incentive to keep cranking out power.

Besides, even in the extremely unlikely event that the firm's plants were shut down tomorrow, there is enough excess generating capacity in Britain to keep the lights on. As that excess fell, wholesale prices would rise. That would cut demand, and encourage generators to revive mothballed plants and increase imports of subsidised nuclear electricity via the interconnector with France.

Anybody want a used nuclear industry?

Since neither the safety nor the supply arguments for spending more taxpayers' money on the company hold water, the government should let it go under. The shareholders will lose their money. That's capitalism. For the future, though, the government should give the nuclear industry a chance to compete by lightening the burden it has placed on the business. British Energy should not, for instance, pay the price of keeping Britain's reprocessing industry going. Nor is the climate-change levy, to which the nuclear industry has to contribute although it generates no carbon dioxide, fairly designed. Nuclear should pay nothing; coal should pay more.

As to who might buy British Energy—what about offering it to France? The poor French taxpayers are so used to having to subsidise their own uneconomic nuclear industry that they might not notice it if they were required to do the same for the British one as well. Worth a try, surely. ■



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Expanding waste

SIR – You say that the solution to the problem of household waste is to get households to throw less away and that this will happen only if consumers are made to pay directly for the waste they generate (“More rubbish”, August 24th). In general, households do not generate waste; they just act as intermediaries between producer and disposer. They do not choose that milk should be sold in disposable packages rather than returnable bottles or that goods come with unnecessary packaging.

Furthermore, the notion that direct payment will reduce waste has been dispelled in Belgium. A swingeing €1.25 (\$1.23) charge per 50-litre bag of rubbish has done nothing to stem the tonnage of waste. Germany may well lead in recycling and composting rates but it is also the leader when it comes to mountains of unusable and unwanted “recyclable” material.

BRUCE GUY
Brussels

SIR – There is a problem with recycling because manufacturers have too little reason to worry about what happens at the disposal phase. Where reasonably possible they should be made fully responsible for recycling their packaging and products. Only then will materials and methods of construction be chosen to minimise environmental costs at the end. If there is a problem with markets for recycled materials then that should be a problem for manufacturers not local councils.

C. OSMAN
Aberdeen

Made in Taiwan

SIR – As a citizen of Taiwan, I do not consider myself Chinese. Gong Jianzhong (Letters, August 24th) will find that a significant portion of Taiwan's population agrees with me. I refuse to be mentioned in the same breath as a nation with a pathetic human-rights record, a stubborn, backward and

selfish political leadership that refuses to step aside and make way for progress, and a suffering population.

China's plan of “reunification” is based on the premise of financial gain. The Taiwanese leadership has some obvious shortcomings but the difference is that the people of Taiwan have the right and freedom to challenge our leaders without fear of retribution.

GEORGE LIN
Sydney

SIR – Mr Jianzhong states that “Taiwan has been an inseparable part of Chinese territory since ancient times.” This is a common misrepresentation that China continually pushes on the world's media. Taiwan has had only loose ties with China throughout modern history. The Dutch were the first to colonise the island in 1622. Before that there was little interaction. In 1662, defeated Ming-dynasty loyalists drove out the Dutch in order to use Taiwan as an offshore base to raid the victorious Ching government in China. The Ching (themselves from Manchuria) finally eradicated the Ming rebels and annexed the island in 1683.

Over the next two centuries, the Ching had little interest in Taiwan. It was made a self-governing province in 1887 only in an attempt to ward off preying foreign powers. In 1895, it was readily ceded to Japan as a war reparations. In 1945, the nationalist government of the Republic of China occupied the island and four years later fled there at the conclusion of the Chinese civil war. The Nationalists maintained power in Taiwan until they were defeated in the 2000 presidential election.

LOREN AANDAH
Minneapolis

India's liquidity problem

SIR – Your article on water rights in India contains a number of misconceptions (“Nor any drop to drink”, August 24th). You correctly refer to the problem of “fuzzy” water rights but then refer to har-

vesting rain and developing watersheds as means of “extending water rights to people who have traditionally lacked them.” In fact, uncontrolled intervention like this, where water is frequently diverted from a legitimate down-stream use, is a classic example of inadequately defined water rights—it is chaotic and unregulated. In Gujarat, a mass programme of “water harvesting” around the city of Rajkot has caused the dam supplying municipal water to dry up.

The water-user associations that you praise are the last thing that will improve water management. First, assess the resource; second, assign water rights; third, define the institutions to administer these rights, which might include water-user associations as a small part of the institutional structure. Starting at the other end of the process, as in Andhra Pradesh, is proving to be a disaster whereby, as you note, the rich and powerful benefit as government agencies withdraw.

CHRIS PERRY
Croyde, Devon

Too many rights?

SIR – Your argument against the Bush administration's restrictions on the rights of suspected terrorists implies that its assessment of the balance between protection of the terrorists' civil liberties and the public's right to liberty from violence has been skewed to favour a “tyranny of the majority” (“A needless victory for terror”, August 31st). However, you do not assess the effects that the administration's actions might have had on the probability of additional terrorist attacks.

Terrorists have always banked on slow moving evidentiary procedures in the courts to evade justice. The Bush administration may have saved thousands of lives through its illegal actions, a benefit that more than offsets their illegality or encroachment on civil liberties. American liberalism has always put life first, before liberty and the

pursuit of happiness. Americans ought not to die because of die-hard liberal ideology.

MITCHELL LANGBERT
West Shokan, New York

SIR – The main purpose of Hong Kong's anti-terrorism measures is to discharge our international obligations in combating the financing of terrorism. The definition of a “terrorist act” follows the international trend by requiring that such an act must fulfil three conditions (“For whom the Liberty Bell tolls”, August 31st). First, there must be the use or threat of action to compel a government or to intimidate the public. Second, the use or threat of action is for the purpose of advancing a political, religious or ideological cause. Third, the act causes serious violence against a person, serious damage to property, creates a serious risk to the health or safety of the public, etc. Actions by individuals or organisations are caught only if they meet all three conditions. Peaceful demonstrations by apolitical organisations will certainly not be affected.

REGINA IP
Secretary for security
Hong Kong

The propaganda battle

SIR – As a non-Arabist satellite surfer, I have found only one channel in the Middle East that is at all watchable (“Towers of Babelaganda”, August 24th). Its morning show typically has attractive footage of heritage sights and city scenes, bright female presenters, news reports with women and men side by side, outdoor concerts of popular and classical music, and overnight news of the English football scene. Catch it while you can; it comes from Iraq.

RICK COLLET
Maidstone, Kent ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James's Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com

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Telephone: +9714 330 0100, Direct: +9714 319 1951, Fax: +9714 330 0311, email: cwhite@difc.ae



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Closing date for applications is 30th September 2002.

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The post of President of the European Patent Office is to be filled as from 1.1.2004.

The President directs the Office; his duties and powers are laid down in the European Patent Convention. He works closely with the Chairman of the Administrative Council of the European Patent Organisation.

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Practical experience in patents and knowledge of the European Patent Organisation would be an advantage.

Appointment is for five years; re-election is possible. The terms of contract will be agreed, prior to election, between the Chairman of the Administrative Council and the nominated candidate.

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Applications must reach the Chairman of the Administrative Council by 31.12.2002 and should be sent under **reference P2004** to:

Mr Yves Grandjean, Director,
Secretary of the Administrative Council
**for the attention of
the Chairman of the Administrative Council**
European Patent Organisation
D-80298 Munich

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International Service for National Agricultural Research

Director General

The International Service for National Agricultural Research (ISNAR) is one of the 16 Future Harvest research centers supported by the Consultative Group on International Agricultural Research (CGIAR). Its mission is to help bring about innovation in agricultural research institutions in developing countries to increase the contribution of research to agricultural development for the poor.

ISNAR is seeking to appoint a new Director General, based at its headquarters in The Hague, the Netherlands. ISNAR has regional offices in Costa Rica, Nigeria, the Philippines, South Africa, and the USA. It has a total staff of 80 and is governed by a Board of Trustees with international membership, to whom the Director General reports as Chief Executive Officer.

Candidates will have a higher degree (doctoral level or equivalent) in agricultural, natural, or social sciences, or in management sciences with experience in agricultural development. They will have proven, relevant senior management experience, preferably in a multicultural, international research or academic environment. For a position offering an interesting and exciting challenge against a backdrop of rapid change in ISNAR and the CGIAR, candidates will have a significant record of achievement and innovation, with experience of living and working in developing countries; they will also have knowledge of national and regional agricultural research systems. Excellent skills in resource mobilization, management, and communication with the scientific and policy communities are essential, as is sound experience in leadership and staff development. They will have outstanding communication and interpersonal skills, with fluency in English, both written and spoken. Knowledge of French and/or Spanish will be a considerable advantage.

Letters of application and curriculum vitae in English, with names of at least three referees and full contact details, should be sent to Douglas D. Hedley, Chair, ISNAR Search Committee, 930 Carling Avenue, Room 309, Ottawa, Ontario, Canada K1A 0C5. E-mail: hedleyd@agr.gc.ca; Fax: +1-613-759-7229.

The closing date for applications is November 15, 2002. A final decision will be taken in March 2003, and the successful candidate will take up duties in July 2003. An internationally competitive salary and benefits package is offered, along with a contract for an initial period of five years.

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ENERGY FOR RURAL TRANSFORMATION (ERT) PROGRAMME

Invitation of Expression of Interest (EOI) for the Post of Executive Director of the Rural Electrification Agency (REA).

1. The Government of Uganda has received a Credit from the International Development Association (IDA) of the World Bank towards the costs under the Energy for Rural Transformation (ERT) programme and it intends to apply part of the proceeds of this fund for the establishment of the Rural Electrification Fund (REF).
2. The REF was established under the Electricity Act 1999 and is to be managed by the Rural Electrification Board (REB). Management of the REF is established by a Statutory Instrument.
3. The Secretariat of the REB is the Rural Electrification Agency (REA), which shall be headed by the Executive Director for whom this invitation for EOI is made.
4. The Executive Director of the REA is the Secretary of the Board. He/She will establish and maintain an efficient rural electrification system; maintain good linkages with key stakeholders (especially the private sector), regularly review rural electrification regulations in consultation with ERA, recommend to the Board on the most efficient utilization of the REF; and oversee the basic planning and preparation of projects by the Agency among other activities.
5. The required person must be a citizen of an eligible country under the World Bank procurement guidelines. Highly qualified Ugandan candidates are particularly encouraged to apply. He/She should be able to work in a multi-disciplinary environment, highly motivated with strong communications and analytical skills, credible in the eyes of stakeholders, and with a good record of management capacity.
6. Required qualifications are:
 - An advanced degree (Masters level) in any of the following fields: Engineering, Economics, Finance, Business Administration, Rural Development, Energy Studies and Management.
 - A degree in an energy related Engineering or Science field followed by a Masters degree in business administration is an advantage.
7. Required experience
 - At least 10 years in rural development
 - Proven skills in developing effective rural energy services with credit facilities.
 - Proven skills in contract negotiations, management of financial resources from bilateral and multilateral development partners.
8. Terms and conditions of service.

Four years contract renewable. Attractive salary and fringe benefits to be negotiated.
9. Expression of Interest (EOI) should be addressed to:

The Permanent Secretary
Ministry of Energy and Mineral Development
P.O. Box 7270
KAMPALA
Email: psmemd@energy.go.ug
Fax: 256-41-234732
Room A115, Amber House Kampala to reach him not later than 3.00 p.m Tuesday 8th October, 2002.
10. Short-listed candidates from respondents to this EOI will be given detailed Terms of Reference against which they will make their formal applications.

F.A. Kabagambe-Kaliisa
PERMANENT SECRETARY

Executive Focus

THE JOHNS HOPKINS UNIVERSITY Center for Communication Programs

Seeks applications from qualified individuals for the position of

Associate Director for Health Sciences

for a global health communication project

Qualified candidates should have at a minimum a Master of Public Health, preferably MD or PhD in the Health Sciences; have knowledge of and experience with a wide range of global health issues; preferably be active in international health panels such as WHO, UNICEF, global funds, and other non-UN advisory groups; be familiar with the major sources of institutional expertise in such areas as HIV/AIDS, maternal and child health, nutrition, reproductive health, tuberculosis, malaria and other infectious diseases; be connected to a wide group of global health experts; be adept at networking and seeking new contacts and partners; and possess excellent interpersonal and oral/written communication skills. Fluency in the English language is required.

Applications must be received by September 30, 2002

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- Leading project engagements.
- Assisting with the management and development of existing Practice staff.
- Writing expressions of interest and full proposals as part of the competitive tendering process to win new projects.
- Recruiting independent consultants as part of the task of assembling project teams.
- Marketing and new business development for the Practice.
- Regular international travel.

The successful candidate for the full time position will be a key member of project teams working on complex reform projects in politically charged environments. Quick on your feet, you'll have the measured professional stature commensurate with this exciting role. Requirements for the full time position ideally include:

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- A demonstrable ability to work with and through others.
- Proficiency in at least one target market language: Spanish, French, Mandarin/Cantonese, Russian.
- An EU national or possession of a UK work permit.

Salary commensurate with experience, but circa £60,000 plus benefits.

The Associate position will entail acting as a short or long term contractor participating in project teams working on utility restructuring, reform, regulation and privatisation assignments in developing countries.

Interested candidates should send a full CV and covering letter by mail or e-mail to:

Stuart King, Adam Smith International, 3 Albert Embankment, London SE1 7SP

E-Mail: stuart.king@adamsmithinstitute.com

The closing date for applications is 5th October 2002.

Northern Maritime Corridor

PROJECT MANAGER

The Northern Maritime Corridor (NMC) is an EU funded international partnership project. It is designed to develop and secure efficient, safe and sustainable sea transport connecting coastal areas of peripheral north-western Europe. The NMC partners are from the Northern Highlands & Islands of Scotland, a range of Nordic countries and North-West Russia.

The Scottish partners wish to recruit a Project Manager for the NMC work. The main tasks will be to:

- Identify and bring together participants in a maritime cluster, including producers, freight forwarders, ship owners, ports, and public bodies.
- Deliver an audit/analysis of the existing position across the various topic areas, utilising external expertise as required.
- Work up action plans with partners to deliver agreed outputs.
- Liaise with partners and other cluster participants in the Highlands & Islands and with international partners as required.

He/she will report to a small executive group of the Scottish partner organisations.

The Project Manager will need to be a flexible, highly motivated person, who can: work under their own initiative to take forward the tasks identified above; and ensure maximum input from stakeholders.

The postholder will be educated to degree level or equivalent, have at least four years experience in project management, and have good communication, negotiating and influencing skills.

Experience in/knowledge of the seafood and/or petroleum industries would be a distinct advantage. Familiarity with the Highlands and Islands and the Nordic Countries and an understanding of the trading links between them is essential, as is a good understanding of logistics/maritime transport.

It is intended that the postholder is based in Orkney. They would be employed by Orkney Islands Council on behalf of the Partnership, at their offices in Kirkwall. The post will be part-time - two and a half days per week - for a period of up to three years. The annual salary will be in the region of £40,000-£50,000 per year, pro rata, depending on skills and experience. In addition, travel and subsistence costs will be paid for travel associated with the project work.

As an alternative to an employee, the partners will consider proposals by consultants to undertake the project management work if at comparable overall cost, and delivering equivalent outputs.

Please apply by sending a covering letter and CV to Christine Madej, Highlands & Islands Enterprise, Cowan House, Inverness Retail and Business Park, Inverness IV2 7GF: telephone 01463 244230, email c.madej@hient.co.uk. A detailed job specification is available from her on application.

Closing date for submitting a job application is Monday 30 September 2002.



THIS PROJECT IS BEING PART-FINANCED
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Executive Focus

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The Graduate School of Management at the University of California in Irvine is uniquely focused on the preparation of future business leaders in a technology-driven, global economy. Offering MBA and PhD programs for 825 students, the School is one of the top 50 business schools in America and is part of a university that is ranked among the top 10 public universities in the country. The School has an excellent faculty and enjoys strong support from a prestigious business community and the parent institution. It is well positioned for advancing to the top 25 status among the nation's business schools.

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Candidates may emerge from the academic, government or business community. Keen intellectual ability will be crucial to lead this academic enterprise. Other key selection criteria will include evidence of: thought leadership in business or economics, external relations and development experience, ability to lead faculty, and administrative management skills.

Applications and nominations, preferably in electronic form, can be sent to gsmrch@uci.edu, or to: GSM Dean Search Committee, c/o Cynthia Hoffman, 535B Administration Building, University of California, Irvine, CA 92697-1000.

UCI is an equal opportunity employer committed to excellence through diversity.



ECON Centre for Economic Analysis is a leading Nordic centre for analysis and research into applied economics. The company has offices in Oslo, Stavanger, Stockholm, Copenhagen and Paris. Much of our work is in the energy sector, and covers market analysis, regulation, environmental economics and industry reform.

Senior energy economist – European energy markets

We are looking for a suitably qualified and experienced energy economist to build and strengthen our portfolio of European projects. The successful candidate would preferably be based in our Paris office, and would work with a team of 4-5 professional economists. Candidates should have a track record in European gas and power consultancy, the ability to manage highly skilled teams and should be interested in the challenge of developing new and existing business areas.

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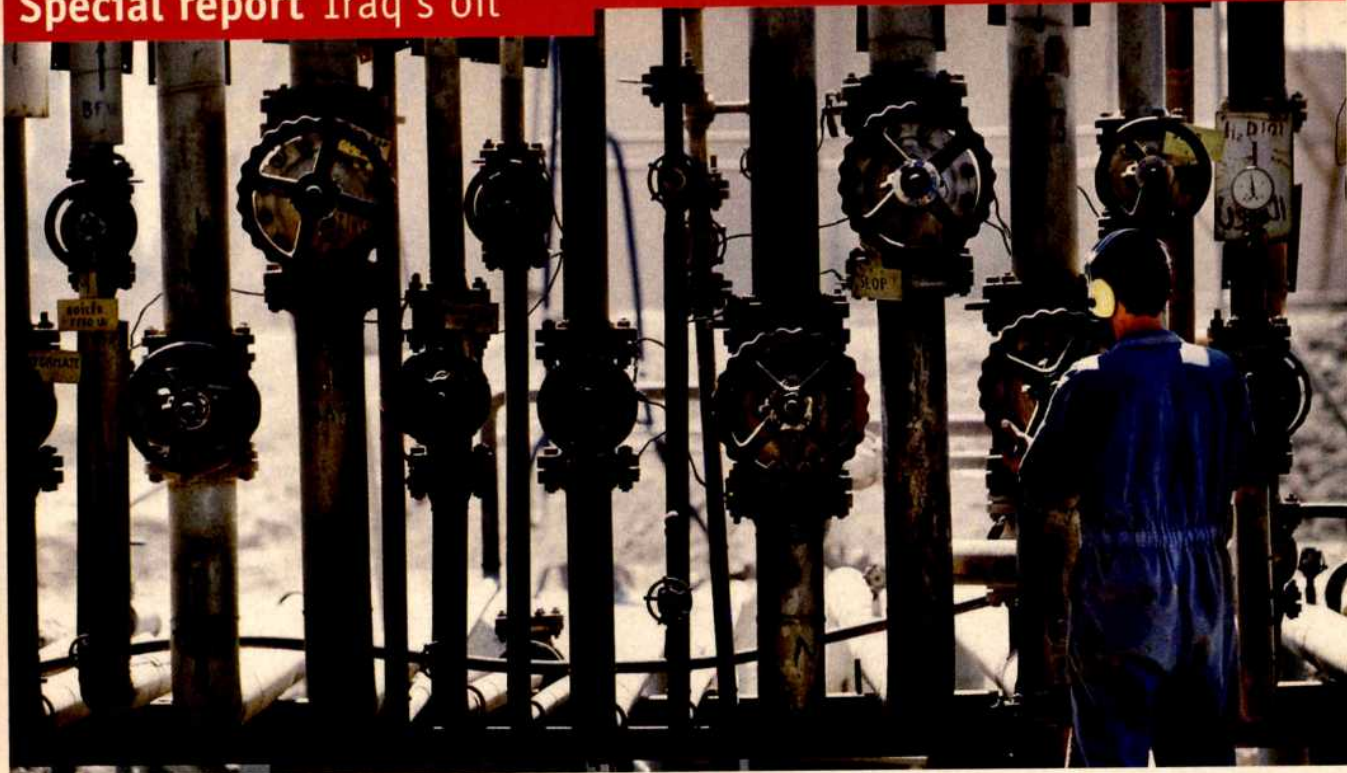
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INVESTOR IN PEOPLE





Don't mention the O-word

If America goes to war against Iraq, what will become of all that oil?

AMERICA'S chief interest in going after Iraq's president, Saddam Hussein, is doubtless to save the world from his actual or potential weapons of mass destruction. Another large consideration, secondary as it may be, has attracted less attention than it should have: the effects that would follow from the opening up of the country's enormous reserves of oil.

Iraq's reserves are the second-biggest in the world, after Saudi Arabia's (see table on next page). At present, thanks to UN sanctions and Mr Hussein's attempts to evade them, the country is producing a fraction of its potential. If it were to produce oil at a rate to match its reserves, say some geopolitical strategists, it could end Saudi Arabia's domination of world oil markets.

That would not come too soon for the United States. America is by far the world's biggest oil-user, burning up a quarter of the total consumed. Its imports have risen in recent years, to more than half its total consumption. Since Saudi Arabia is the chief supplier of those imports, successive American presidents have gone to great lengths to cultivate the unsavoury and dictatorial House of Saud. They have also tolerated Saudi Arabia's command of the

Organisation of Petroleum Exporting Countries (OPEC), which keeps oil prices much higher than they would be if market forces prevailed. Now America's leaders increasingly feel—as Winston Churchill remarked of converting the British fleet from coal to petroleum before the first world war—that “safety and certainty in oil lie in variety, and variety alone.”

In hopes of finding such variety, George Bush is now changing American policy. He has openly embraced Vladimir Putin's goal of expanding Russia's oil industry, with talk of increased exports and a big ministerial conference on energy planned for Houston in October. Another opportunity, openly acknowledged or not, is the present showdown with Iraq. Rumours of war are likely to dominate the meeting of OPEC ministers on September 19th in Osaka, in Japan.

The fear premium

Conventional wisdom says war drums are good news for OPEC and the Saudis today, but bad news in the longer term. Talk of war always heats up the oil price, giving producers an instant windfall. Yet tomorrow, if America succeeds in toppling the bully-boy of Baghdad, the world could be

awash in Iraqi oil. Look closer, and matters are more complicated.

In the short term, jittery traders are already handing oil producers a handsome windfall profit. Last week, on ill-founded rumours of a huge air strike by American and British planes in western Iraq, prices shot to their highest level in a year, passing \$30 a barrel for West Texas Intermediate, America's benchmark crude. Daniel Yergin, head of Cambridge Energy Research Associates (CERA), an industry consultancy, estimates that the “fear premium” on each barrel of oil is now \$3-5.

As war gets closer, prices seem bound to go higher. During the Gulf war, a decade ago, prices spiked past \$40 a barrel in nominal terms. Phillip Ellis of the Boston Consulting Group, who has analysed the history of oil shocks and their impact on prices, argues that prices fall into two ranges. The peace curve, as he calls it, “forms around an average of about \$22-24 in today's money. The war curve forms around a price north of \$50.”

Some would put it higher. Sheikh Zaki Yamani, Saudi Arabia's oil minister during the shocks of the 1970s, gave warning last week that if America invades Iraq, Mr Hussein could attack Saudi Arabia and Kuwait and so send oil prices to \$100 a barrel. Iraq's vice-president, Taha Yassin Ramadan, stirred the pot further this week by goading fellow Arabs to strike American targets in the Middle East if Iraq is attacked.

High prices are clearly a nightmare for consumers. Paradoxically, and here is where the complications begin, they are bad news for producers, too. Prices much above Mr Ellis's “normal” range act as a ▶

Lagging behind

Crude oil, at end 2001

	Reserves bn barrels	Production m barrels per day
Saudi Arabia	261.8	8.8
Iraq	112.5	2.4
UAE	97.8	2.4
Kuwait	96.5	2.1
Iran	89.7	3.7
Venezuela	77.7	3.4
Russia	48.6	7.1
United States	30.4	7.7
Libya	29.5	1.4
Mexico	26.9	3.6

Source: BP Statistical Review of World Energy

► brake on economic growth. There are signs of this happening already, especially in Asia. Some economists worry about an oil-induced global downturn. As the earlier oil shocks have taught OPEC, prolonged periods of high prices only kill the goose that lays the golden egg.

Another reason why sky-high prices are bad for OPEC, and especially for Saudi Arabia, is that they spur oil production from uneconomic places. In a genuinely free market, most of the world's oil would be produced by Saudi Arabia and its neighbours, where the cost of exploration and production is a dollar or two a barrel. In contrast, trying to force drills through rocks in the Arctic or beneath deep water can heap up costs to \$10-12 a barrel.

Getting round the Saudis

Because OPEC's "price-defence" strategy has kept prices above \$18 a barrel for three years, argues the Petroleum Finance Company (PFC), an industry consultancy, projects in non-OPEC regions—the frozen wilds of Russia, the turbulent Caspian basin, the deep waters of the Gulf of Mexico—have attracted many billions of dollars in investment. High prices have already inspired the development of 2.6m barrels per day (bpd) of non-cartel oil, besides investment in projects that promise to deliver another 5.2m bpd from alternative sources by 2008. This new supply, says the PFC, "has and will continue to eat up all the increase in global demand, leaving OPEC no room to expand its own output and making the cartel's price-defence strategy increasingly difficult to maintain."

However, the pain is not equally shared among cartel members. It is felt mostly by Saudi Arabia, the self-appointed "swing" producer. That is because higher prices have also encouraged some of the smaller fry in the cartel, such as Nigeria, Algeria and Libya, to develop new production capacity and to bypass existing production quotas set by OPEC. John Mitchell, an energy analyst at Britain's Royal Institute of International Affairs, of-

fers a more fundamental reason to suppose that the cartel's "aggressive collusion" will not endure: the ratio of production to reserves varies greatly among cartel members, and so the incentive to increase output rather than keep it flat also varies greatly.

The result, according to estimates by Deutsche Bank, is that new supply could outstrip expected demand by as much as 1m barrels a day by 2004. The only country that has historically been willing to reduce its own output—and revenue—by such a large volume to "balance" the market and prevent a price collapse is Saudi Arabia.

All this explains why Saudi Arabia has long advocated a moderate stance on prices. Yet when ministers meet in Osaka next week, they face a dilemma. Thanks to fears about war with Iraq, prices are high and the markets are anxious. Winter is on the way, and with it a seasonal upturn in demand for oil. On September 11th the International Energy Agency (IEA), a quasi-governmental watchdog set up by the world's biggest oil consumers, said that stocks of crude were "uncomfortably low" going into the winter, and the whole situation "every bit as precarious" as in 1999, before a notably volatile spell for oil prices.

This being so, the Saudis might argue at Osaka for a modest increase in quotas. On the other hand, as Venezuela and Iran point out, the greatest risk facing the cartel is not high prices but a price collapse. That could happen if OPEC releases oil into a weakening global economy. It did precisely that in the run-up to the Asian economic crisis a few years ago, and oil prices fell to around \$10 a barrel.

Even if Saudi Arabia somehow smooths over the meeting in Osaka, some argue, the longer-term picture for the cartel is bleak. The expulsion of Mr Hussein, which looks likelier than not, could turn the oil market upside down. This is because Iraq, with its vast reserves, is the only country that could challenge the Saudis by throwing open the taps.

If a post-Saddam regime did that, Saudi Arabia's strategy of keeping OPEC prices

between \$22 and \$28 a barrel would be under threat. If the flood of Iraqi oil continued indefinitely, goes the argument, the Saudis would have no choice but to abandon price (and, with it, their allies in OPEC with higher costs and smaller reserves) and go for volume instead. Though politically difficult, that need not be economic folly: Deutsche Bank calculates that Saudi Arabia could maintain oil revenues at \$60 billion or so either by producing 6m bpd at around \$30 a barrel, or by cranking out 10m bpd at about \$17 a barrel.

Will the flood of Iraqi oil occur? It is possible. Any future government in Iraq, needing vast amounts of money to rebuild the country, will try to expand the oil sector as fast as it can. At least some oil executives believe that this bonanza could draw much foreign capital into Iraqi oil production. Even if the new government did not break ties with OPEC, as the United States might like, it would probably argue—bearing in mind the years of UN supervision of its oil exports—for a lengthy exemption from quotas.

OPEC, RIP?

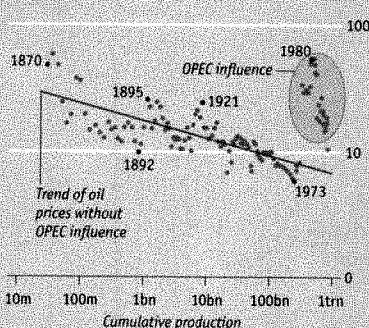
It might seem, then, that knocking out Mr Hussein would kill two birds with one stone: a dangerous dictator would be gone, and with him would go the cartel that for years has manipulated prices, engineered embargoes and otherwise harmed consumers. Yet several factors suggest that the transition to a post-Saddam oil world will be messy—and that such a world could still have a forceful OPEC in it.

Consider again Sheikh Yamani's fear: that Mr Hussein, in a desperate last act, may attack the Saudi and Kuwaiti oil infrastructure and bring the global economy to a halt. The oilfields could be set ablaze, as they were during the Gulf war. Refineries and terminals could be contaminated with radioactive or biological agents. With help from outsiders, Mr Hussein might be able to shut down shipping lanes such as those in the Straits of Hormuz, preventing Saudi Arabia from getting its oil to market.

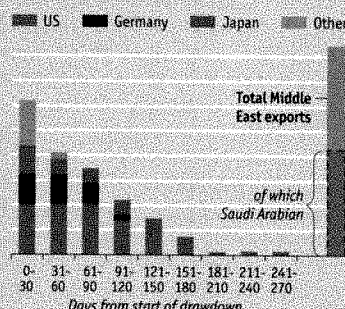
On balance, though, the risks of a pro-►

The OPEC effect

US average oil price, 1998 \$ per barrel



Source: Boston Consulting Group

Vulnerable stocksOECD strategic oil reserves
m barrels per day available for release

Sources: Deutsche Bank; BP

Iraq's oil exports

Strangled

The UN gets tougher still

THE mere threat of an invasion is already squeezing Saddam Hussein in at least one way: money. His oil exports, which the UN supervises as part of an oil-for-food scheme, are collapsing. Last year, Iraq exported an average of 1.7m barrels per day (bpd) under the UN programme. Earlier this year, that fell to 1.2m bpd; last week, it was 370,000.

In the past, Mr Hussein has often slashed or raised output to make war noises of his own—suddenly trying to shut off all UN exports, for example, when the Israeli-Palestinian conflict became more deadly, in hopes of inciting a broader Arab oil embargo. Such volatility also gives him leverage with OPEC, as the cartel never knows how much Iraqi oil to expect.

The reasons for the latest decline are different, however. The UN has decided to crack down on Mr Hussein's main

way of profiting from his oil. In the past, he managed to persuade middlemen (many of them Russian) to pay an illicit surcharge, direct to him, of around 25 cents a barrel. The UN is trying to cut out those middlemen, and has recently introduced a retroactive pricing scheme: buyers must first commit to a shipment of oil, and will find out only later what price the UN has imposed. This stamps out the surcharge, but few buyers—especially the Americans, once big customers—want to take the risk of buying oil without knowing the final price.

The tyrant is not left destitute. Deutsche Bank estimates that Mr Hussein still manages to export perhaps 400,000 bpd to Jordan, Syria and Turkey via pipeline and lorries; he smuggles some in “tanker caravans” through the Gulf. Such exports are deeply discounted, but still brought him perhaps \$2 billion in 2001.

Americans. The result could be chaos in the world markets, and OPEC left firmly in control.

Another reason to doubt that an invasion would kill off OPEC is the state of Iraq's oil infrastructure. Thanks to a dozen years of UN sanctions, and many more years of mismanagement and over-exploitation, the country's petroleum industry is in pitiful shape. Even in its best times, the country produced only 3m-3.5m bpd: a third of Saudi Arabia's peak and half of Russia's. As one American oil executive says, “Under the very best scenario, Iraq might manage that peak again.” To do better, the country would need massive investment from the world oil industry.

Expect no miracles

That, says the same senior oilman, will be slow in coming until companies are sure that the new regime will be stable and will respect the rule of law. Realistically, experts say, it will take Iraq perhaps five years of hard work, western know-how and big money to turn its oil industry into a serious force again. CERA puts it bluntly: Iraqi output can only increase from today's low levels, but that does not mean “a massive, rapid increase in production that will depress prices, displace other Gulf producers and render OPEC impotent.”

In short, a “regime change” of the sort that Mr Bush has in mind for Iraq might rewrite all the rules of the oil game—on paper. The president's new friendship with Mr Putin also heralds an important change in the geopolitics of energy. In practice, however, the second Bush to take on Mr Hussein will probably be long gone from the White House before the oil markets are transformed by Iraqi oil. Don't write off Saudi Arabia, or OPEC, just yet. ■

longed physical disruption seem small. One senior European oilman insists that it would be very difficult to engineer a complete shutdown of all Middle Eastern oil: “That's a bit like thinking you could shut down all North Sea production by firing SCUD missiles from Germany.” CERA's Mr Yergin says it is difficult to target all the oil fields, pipelines and export terminals that matter in the area. Saudi Arabia has plenty of spare capacity and transport options for its oil; besides, pipelines are pretty quickly patched up.

The world also holds emergency stocks of oil much bigger than those it held back in the 1970s. These should not inspire complacency; as the chart on the previous page shows, they cover only a few weeks of disruption, and a prolonged war could still mean disaster. Yet the world at least has the IEA, monitoring oil markets and emergency stocks and engaging OPEC in “consumer-producer dialogues” (another one will take place in Osaka next week) to encourage stable prices. If oil supplies are suddenly threatened, as Robert Priddle, the IEA's boss, explains, governments have even given him the extraordinary power to release oil stocks unilaterally.

Fears of a physical disruption to supply are therefore overblown. More worrying, however, is the possibility that Saudi Arabia will decide it does not want to get extra oil to market. Historically, the Saudis have always acted as the market's guarantor of last resort. During the Iran-Iraq war, for example, they stepped into the breach and increased output to smooth prices. As they

intentionally keep a whopping 3m bpd or so of spare capacity to hand, their country alone can easily compensate for the loss of Iraq's current output.

But the Saudis do not like the way the Bush administration is setting about Iraq. The regime also faces great anger on the “street” for its cosiness with the American government. Add to that the Saud dynasty's precarious grip on power, and the ruling family might find it politically impossible to crank up production to help the



With years of graft and heaps of money, they may be a force again



Kashmir's elections

A terrible beginning

KUPWARA, SRINAGAR AND DELHI

On the eve of voting, a law minister is shot dead

SOME trappings of a normal election are there. Buses bristling with megaphones and party flags barrel along the roads; dancers and drummers attend the candidates at village rallies. Lurking nearby, though, are camouflaged men with guns, and they are needed at this time. On September 11th, Mushtaq Lone, a candidate for the ruling party in the elections for the state assembly of Jammu and Kashmir, was shot dead along with six of his companions.

Mr Lone, the state's law minister, is the most prominent victim yet of Pakistan-based militants who are trying to disrupt the elections. Their ultimate purpose is to wrest India's only Muslim-majority state from its control. Mr Lone's murder raises the risk that the elections, which are to begin on September 16th, will not meet what is probably their most important objective: convincing India to resume talks with Pakistan after a breakdown in relations that pushed the nuclear powers to the brink of war this summer. India has made it clear that it will judge Pakistan's fitness for dialogue by the level of election violence.

The second electoral goal was already a lost cause: persuading separatist politicians to enter the democratic mainstream,

to press their cause from the platform of the state assembly. There is a chance to salvage a final one: to prove that India can hold free and fair elections in a state where vote rigging has come to symbolise everything people hate about its rule.

Failure would reverberate widely. Colin Powell, the American secretary of state, said in Delhi in July that credible elections could be a first step toward peace in Kashmir and dialogue with Pakistan. In his remarks some Kashmiris saw hope. They have had their fill of war, which began 13 years ago as an indigenous rebellion against Indian rule and is sustained now by imported militants, who often indulge in sheer terrorism. Their crimes provoke brutality by Indian security forces. "We are facing two guns," as a villager in Mr Lone's Kupwara district puts it. Many are also fed up with the National Conference party, which has ruled for the past six years and headed most of the state's elected governments. They think it achieved power through rigging elections and has done little with it but enrich its bosses.

Most Kashmiris in the Valley, the Muslim dominated part of the state, scorn both India and Pakistan: they want *azadi*, independence. If cynical Kashmiris turn out to

vote, it will be in part because they think the Americans are looking on. "We are fighting elections on the assurance given by the Americans," says Muhammad Amin Khan, a jobless man in a Kupwara village. "If they don't lead to a solution in Kashmir, there will be bloodshed."

The United States wields influence only on the governments of Pakistan and India, and they have been resistant. Pakistan's dictator, Pervez Musharraf, condemns election violence, including the murder of Mr Lone, but outfits based in his jurisdiction are its most zealous practitioners. In May Pakistan-based militants murdered Abdul Gani Lone, a moderate separatist who was thinking of taking part. If the Kashmir elections are farcical, as General Musharraf has claimed, it is in part because groups operating under his nose are making them so. If this gets bad enough, India may refuse to talk to Pakistan and might even resume making warlike noises.

K. Rajendra Kumar, inspector-general of the Kashmir police, insists that infiltration by militants across the line of control, which divides the state into zones controlled by India and Pakistan, is as high as ever, despite General Musharraf's promises to stop it. The government in Delhi had been keeping an open mind about whether to talk to him after the elections, but outrages such as the murder of Kashmir's law minister are bound to shut it.

India, too, bungled its democratic prep work. It says that the separatists who decided to sit out the elections are beholden to Pakistan, tempted by its cash and frightened of its guns. But India's inducements were niggardly. Three top leaders of the

Also in this section

26 Dangerous Afghanistan

27 Australia treasures the backpackers

27 Escaping from North Korea

28 AIDS in China

28 Corruption in Vietnam

► All-Party Hurriyat Conference, the main separatist grouping, are in jail. India hinted that it would suspend the state government during the election to reduce the risk of rigging, then backed away for fear of offending the chief minister, Farooq Abdullah, whose National Conference party is part of the coalition that governs in Delhi. Any separatist who stood for election risked looking like a stooge, which might have been India's hope.

The Hurriyat is boycotting the polls, though unenthusiastically. A few pro-*azadi* candidates are contesting, but the bulk of the opposition is a motley, but largely pro-Indian collection of independents, defectors from the National Conference and mainstream parties, such as the Congress party. The voting could thus be perfectly free and fair without reflecting the will of the electorate. That does not mean the election will be a non-event. Resentment against the National Conference may be running high enough to topple it, which could bring in a government that is fractious but on better terms with the electorate. The party is fighting back with a new leader, Omar Abdullah, Farooq's son, who is bright, young and does not have enough of a track record to have disappointed the voters. It is well organised and will benefit if the turnout is low.

If an Abdullah scrapes back in, the six years of the next assembly might be a lot like the last, especially if the Indian government sticks to its line that it will talk only to Kashmir's elected representatives. There are hints that it may not. A committee of notables, which claims government backing, has lately been talking to Hurriyat leaders. One of them, Mirwaiz Umar Farooq, suggested on September 10th that they might settle for autonomy within India. This does not appeal to most Kashmiris, who have seen autonomy granted and then snatched away before. It seems scant recompense for the 30,000-70,000 Kashmiris who have died in the insurgency. But it might be made palatable by guarantees and amends for past abuses.

The decision, though, rests with India and Pakistan. Both countries' leaders were due to speak to the United Nations' General Assembly this week, General Musharraf on Thursday and India's prime minister, Atal Behari Vajpayee, on Friday. Some new thinking on bringing peace to Kashmir was hoped for. Autonomy would preserve India's territorial integrity, its highest priority; just possibly, it would allow Pakistan to claim credit for securing Kashmiris' self-determination. If they were reasonable, the Indian and Pakistani governments would agree on autonomy in some form. If the governments were honourable they could persuade Kashmiris that they were safe in settling for it. But neither government has displayed much reason or honour on Kashmir. ■

Afghanistan

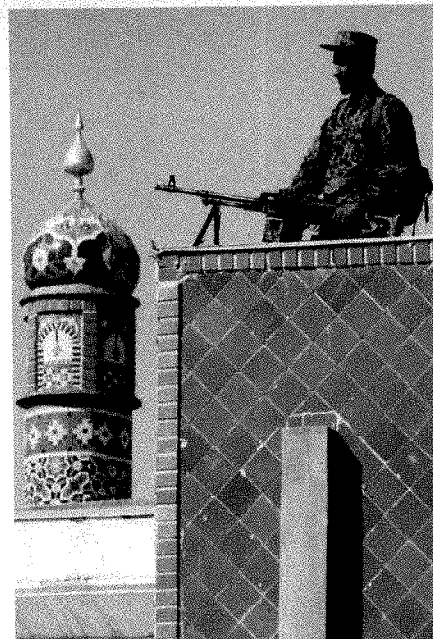
Insecure

Suddenly, even the capital is dangerous

IN THE streets of Kabul, the usual maddening traffic has thinned. The many Afghans who were this week commemorating their own national disaster, the murder a year ago of Ahmad Shah Masoud, leader of the only group to hold out against the Taliban, mostly decided that the capital was too dangerous a place to linger in for long. On September 5th, a bomb placed in a crowded area in central Kabul killed at least 25 people and injured another 170. On the same day, President Hamid Karzai narrowly escaped assassination in Kandahar: a gunman who had recently joined the local governor's security forces opened fire on the president's car with a Kalashnikov, missing him by inches. And in the south-east, a renegade warlord is once again making trouble. The past ten days have been a blunt reminder that, although Afghanistan has come a long way over the past year, security remains elusive.

In Kabul, security has been stepped up, with the International Security Assistance Force (ISAF) providing more patrols, and Afghan forces searching cars for weapons and explosives. More than 15 people have been arrested in Kandahar in connection with the assassination attempt on Mr Karzai, but it is unclear whether they were involved. The would-be assassin was shot dead by an American bodyguard. Most earlier crimes, among them the murder of a vice-president and the tourism minister, remain unsolved.

There is no shortage of suspects. Afghan officials have been quick to blame al-Qaeda or the Taliban for the attacks in Kabul and Kandahar, while hinting that Gulbuddin Hikmatyar, an unpopular prime minister in pre-Taliban times, may also be involved. On September 4th, Mr Hikmatyar repeated a call for *jihad*, while denying he had linked up with the al-Qaeda network and the Taliban. Although most people, including the Afghan administration and American defence officials, seem to agree that the Taliban and their al-Qaeda protégés are no longer an organised force in Afghanistan, they can still destabilise the fragile Afghan government through attacks on well-chosen targets. American intelligence officials claim, according to reports, that al-Qaeda fighters who fled to Pakistan are moving back into Afghanistan in small groups. Coalition forces have just launched another anti-terrorist operation, optimistically dubbed Champion Strike, in Paktika province.



Not an ornament

But some in Afghanistan, among them diplomats, soldiers and aid workers, believe that political rivalry may be at the root of many recent incidents. Mohammed Fahim, the powerful Tajik defence minister, is said to be under pressure to lessen his grip on the country's security apparatus, and in particular, the National Security Directorate (NSD), the secret police. Security scares have been frequent in Kabul. Many preceded last week's carnage. Continued worry over security is clearly in the NSD's interest and will be an argument against lessening its powers. Many Afghans marvel at the fact that NSD officers always seem to be present at the scene of incidents before ISAF soldiers arrive.

Mr Fahim has staffed the NSD with fellow Tajiks, a tribe from the north, to the displeasure of the southern Pushtuns, the largest ethnic group in Afghanistan and its traditional rulers. Some believe the attempt to kill Mr Karzai may have been motivated by such grievances.

Then there is the problem of the warlords, wrestling for regional control. On September 8th, fighting flared in Khost, where Pasha Khan Zadran, a warlord who has been supporting the coalition's military operations locally, is now trying to establish control over the region. He was appointed governor of south-eastern Paktia province last December, but was unable to take office there after the local population made it clear his past was too shady for their taste. Another governor was then appointed. Mr Zadran moved to neighbouring Khost, where he has been challenging its governor, Hakim Taniwal. In recent clashes 15 people have died and over 50 have been injured. Mr Zadran denies he has retreated to the mountains and says he is still fighting for control of the city. ►►

There is no quick way to secure the country. The United States and other countries are helping the Afghan government to build a national army and police, which will, they hope, bring order to the whole of Afghanistan. In the meantime, Mr Karzai has repeatedly asked for ISAF to be expanded beyond Kabul. After insisting for months that there was no need for this, American defence officials are now saying they would welcome such a move. A permanent presence in the main Afghan cities, or a mobile force based in Kabul, would not turn Afghanistan into a haven of peace, but it would certainly help. But while America now goes along with the idea, it will not provide any troops. According to Victoria Clarke, speaking for the Pentagon, other countries will have to come up with the necessary.

The problem, however, is how to find volunteers. On September 8th, Francesc Vendrell, the European Union's envoy to Afghanistan, declared that the expansion of the peacekeeping force outside Kabul was "virtually impossible at the moment" because European governments do not have the resources. For now, it is even unclear who will take over after Turkey, which currently heads the 4,700-strong force, completes its mandate in December.

Meanwhile, there is Mr Fahim and his ambitious secret police. A western diplomat in Kabul reckons that he is a real enemy of peace. The diplomat accepts that you have initially to work with the enemy. "For the coalition to fight the Taliban, you need the help of warlords and Fahim. But this is not good for the long- or even medium-term stability of Afghanistan." ■

Australia

Saved by the backpackers

SYDNEY

While tourism slumps, the young still travel

AFTER Sydney staged the Olympic Games to acclaim two years ago, Australian business leaders sat back to wait for the tourism boom they believed must follow. They are still waiting. Their anxieties were heightened last week when Joe Hockey, the tourism minister, chided the industry for failing to capitalise on the Olympics publicity. The number of international tourists coming to Australia had fallen by 10% over the past year, he said, a loss of A\$2 billion (\$1.1 billion). Many tourists are choosing to go instead to places such as Canada, Singapore and, most gallingly, Botswana.

The downturn is particularly worrying because tourism has come to be seen as one of the economy's big hopes. Twenty years ago, it was of little importance. Australia's distance from the rest of the world, and vast distances within the country, made it an exotic place out of most people's reach. Then came the opening up of locations such as Kakadu National Park in the Northern Territory and the rainforests of north Queensland, the boom in adventure travel and "eco-tourism", and the growth of Sydney as a world-class city. The deregulation of the economy and its exposure to globalisation forced Australians to diversify. Selling the country as a tourist destination became a frontier industry. Tourism is now the fourth-biggest export earner.

Tourism slumped worldwide after the terrorist attacks of September 11th last year. The collapse three days later of Ansett, one of Australia's two main airlines, temporarily cut off connections to some outback destinations. But Mr



Warmly welcomed

Hockey blames the tourist industry itself for much of the downturn. Botswana, he says, has proved more competitive than Australia at marketing itself as an adventure destination. But in Sydney some shopkeepers point out that Australia has had bad publicity, particularly in Europe, over the federal government's detention of asylum seekers in outback camps. It suggests an Australia far different from the easygoing, welcoming country of the Olympics period.

Still, there are the backpackers, who continue to flock down under in a big way. They stay months rather than weeks and spend their last dollar. Brigid Flynn, manager of the Biltmore on Bondi, a backpacker hotel facing Australia's most famous beach in Sydney, says her biggest worry is not falling numbers but a growth of illegal backpacker hostels poaching her customers. "People of 19 or 20 years aren't rattled by images of September 11th or imprisoned asylum seekers," she says. "They just travel."

North Korea

Escape to the South

SEOUL

The long and dangerous route to safety

A YOUNG North Korean who had escaped to China wrote to Chun Ki-won, a South Korean missionary, to say he was thinking of setting fire to himself in Beijing's Tiananmen Square. This, he said, would draw attention to the plight of those like him who desperately wanted to get to South Korea. Mr Chun has become known in the Koreas as a man who has worked to provide an escape route from the North to the South. He has risked his life—and has spent time in a Chinese jail—to bring 170 northerners to South Korea by way of Mongolia, Thailand and Cambodia. But many thousands of North Koreans still live in China in fear of being caught and deported back to the North.

Mr Chun persuaded the northerner to scrap his suicide plan and to try to defect to the Ecuadorean embassy instead. But the Chinese authorities learnt of the plan and arrested the northerner and seven of his companions. It is not known what has happened to them. At least Mr Chun may have saved the man's life. In all his years of helping refugees, 46-year-old Mr Chun had never before come across such a threat. But a South Korean government official says that unless the refugee problem is solved, a suicide should not be ruled out.

More than a dozen non-governmental organisations and hundreds of missionaries are working separately to rescue the northerners, and some may be tempted to go for a shock protest to gain media attention. The government official insists that quiet diplomacy is preferable. Nearly all the defectors who have managed to get into the embassies or other foreign establishments in Beijing and other cities have eventually made it to South Korea. Whatever its comradely links to North Korea, the Chinese government wants to be seen as humane, despite reports that it has treated Koreans brutally in border areas. This week 15 North Koreans who sought refuge in a German school in Beijing were allowed to leave for South Korea via a third country, believed to be the Philippines.

In the end, it is the North Korean regime that must ease the refugee problem by reforming its economy. There are signs that it is trying to do that by being flexible over wages and prices and introducing an incentive system at factories and farms. But a free market it is not. Any financial freedom in the country is in the growing black economy, based on dollars, which are never banked but kept at home. ■

China

Owning up to AIDS

A "state secret" is revealed

THE government of China said on September 6th that by the end of the year at least 1m of its citizens will be HIV-positive, the condition that can lead to AIDS. Although China has been acknowledging over the past year that it has a problem with the disease, this is the first time it has admitted its extent. The figure is in line with a United Nations estimate in June of between 800,000 and 1.5m.

The epidemic seems to be particularly widespread in the northern province of Henan. In a government report published on the Internet in August by a doctor, Wan Yanhai (who was later arrested for "revealing state secrets"), Henan health officials admitted that state-sponsored "blood stations" had exposed hundreds of thousands of people to the HIV virus. Blood was taken from donors for \$5 a bag without suitable safeguards in place, and recycled. This practice, combined with the use of unsterilised equipment, led to an HIV infection rate of 35-45% in some villages in the province.

While the government's new candour has been widely welcomed, there are doubts about China's financial means and technical ability to tackle the epidemic. The country has only 20 or so experts with a knowledge of international experience in dealing with HIV/AIDS. Many more are thought to be needed to devise and implement a useful campaign.

The cost of treatment also remains high. Reports that the government had threatened to produce copies of patented HIV medicines were quickly denied by China. But the government says it has started treating patients with a domestically produced version of AZT, for which patents recently expired, and that ten Chinese firms have applied for permission to make versions of other HIV drugs with expired patents.

A modest five-year nation-wide plan was set up last year, designed to combat AIDS by focusing on prevention, and improving the safety of donated blood. But two AIDS researchers, Joan Kaufman and Jun Jung, authors of a report on the disease in *Science*, an American magazine, argue that the fight against AIDS in China should take place primarily at a local level. Provincial officials have tended to play down the spread of the disease for fear of losing foreign investment, and have been complicit in private blood collection. Students currently receive little formal sex education

beyond advice to abstain, and have limited access to reproductive health counselling and services. Public understanding of the nature of the virus, and how it is spread, is limited.

A survey conducted by a newspaper in the southern province of Guangdong found that even in a prosperous part of China, almost half of those aged 20-64 did not think that condoms protected against AIDS, and more than half the respondents thought that it could be contracted through sneezing and shaking hands. Given such misinformation, China will need to work hard to catch up with one of the world's biggest medical problems. ■

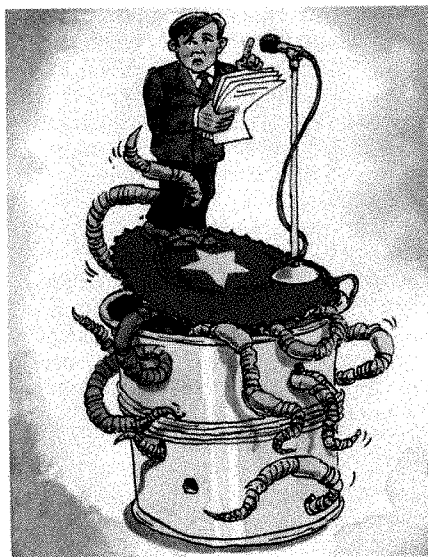
Vietnam

Corruption abounding

HO CHI MINH CITY

The issue that could undermine the government

THE Vietnamese have never seen anything like it: more than 100 government officials arrested, some 50 police officers suspended from duty, and two members of the all-powerful Central Committee expelled from the ruling Communist Party. It is hard to find an official in Ho Chi Minh city, it seems, who was not in cahoots with Nam Cam, a local crime boss. Over the past eight months, a much-publicised investigation has implicated public prosecutors, prison wardens and journalists, among others, in the gangster's drug, prostitution and protection rackets. The arrests are proof, say Vietnam's rulers, that they are serious about fighting corruption, which has spread since the introduction of market reforms in the late 1980s. In fact, the government's attitude is not so clear-cut.



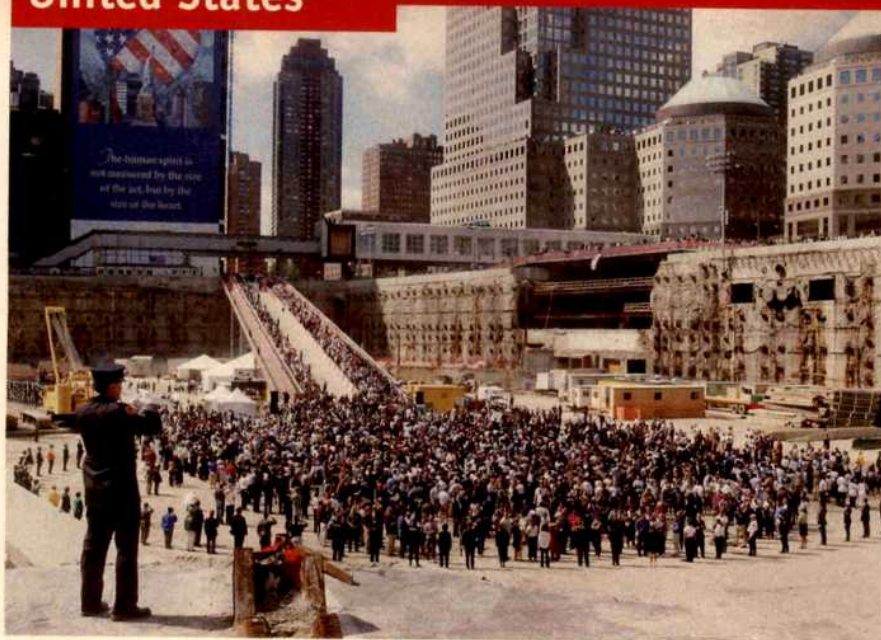
But the scandal certainly is proof of how widespread corruption has become, and how hard it will be to uproot.

Transparency International, a global counter-corruption watchdog, ranks Vietnam as the second most corrupt country in South-East Asia (after Indonesia), based on a survey of international businessmen. The Vietnamese government itself recently estimated that light-fingered bureaucrats cream off at least 20% of infrastructure spending. At the National Assembly in July, the prime minister, the speaker, and the secretary-general of the Communist Party all identified corruption as one of the government's main challenges.

With good reason: ordinary Vietnamese gripe about corruption far more often than they do, say, about the regime's restriction of political freedoms. It is the chief rallying cry of dissidents, and the most frequent cause of popular protests. The party's chief ambition, now that it has abandoned Marxism, seems to be the maintenance of its own power. Public disenchantment brought on by corruption is one of the biggest threats to that cause.

Yet the regime's response so far, whatever its public stance, seems half-hearted. Suspicions persist that the Nam Cam affair might go even higher than the two Central Committee members—but the investigation will not. There is no reason to imagine that Ho Chi Minh is the only big city with greasy-palmed apparatchiks, but there is no sign of a crackdown elsewhere. A deputy prime minister, sacked for corruption in 1999, is back in an advisory role. Proposals for legal reform will take years to implement. The cautious government still allows only a summary of its budget to be published, and is even dragging its feet over a proposed survey, to be paid for by a Swedish government agency, to establish just how widespread corruption is.

The cynical explanation for all this holds that the government is simply doing the minimum to dispel public anger. More charitable observers insist that it is genuinely determined to tackle corruption, but in the same cautious, consensual manner with which it has approached every sensitive subject from the adoption of market reforms to the restoration of ties with the United States. Those two steps, however, pandered to the interests of senior officials—many of whom have businesses on the side—by expanding the scope for private enterprise. This time around, the opposite is the case: the same officials who commit many of the abuses will now be charged with putting a stop to them. Appointing an independent anti-graft agency would be anathema to the party, which insists on preserving a parallel bureaucracy to enforce its will over the main one. On corruption as with all pressing issues, the party faces the same paradox: to preserve its power, it must relinquish some. ■



New York city one year on

A tale of two cities

NEW YORK CITY

There is one New York that is recovering well from September 11th—and another New York that probably never will

"BACK to business as usual" was the rallying cry taken up by New Yorkers a year ago, after terrorists destroyed the World Trade Centre. Remarkably, a sort of normality has returned to the city. The first few months after the attack were dreadful, but the new year brought new hope, tourists and businessmen started to return, the hotels and Broadway shows began to fill up. This summer, the city's economy has reportedly resumed growth after a deep recession.

Even so, it would be wrong to conclude that life has returned to normal. New York is not over the terrorist attacks yet, and may never be. It remains consumed with grief for the thousands of lives lost, remembered this week in countless services throughout the city—big and small, private and public. The most moving was the reading of the names of each murdered individual, which came just after one minute's silence was observed at 8.46am on September 11th, the exact anniversary of the first plane hitting the first tower. Can New York ever have been so quiet?

It was a revealing silence, combining both remembrance of what happened with a fear of what might be yet to come. The fear of another attack has been nagging away at New Yorkers throughout the past year, more often privately harboured than publicly acknowledged.

There was a brief moment of collective panic around Memorial Day in late May,

after the federal government started sharing its fears that terrorists might target cities with weapons of mass destruction and the *New York Times Magazine* ran a cover story exploring what might happen if a dirty nuclear bomb went off in Times Square. But this week's ceremonies have pushed these fears once more to the forefront of people's minds.

How can New Yorkers achieve the "closure" most of them yearn for when they know that those who took their friends and colleagues could at any moment come back for them? There will be a collective sigh of relief once this anniversary week has been (hopefully) safely negotiated. But most New Yorkers will not forget that what made the city such an attractive target a year ago continues to make it the likeliest focus for any future attack in America.

A year ago, it was routine to say that the city, along with the world of which New York is the self-proclaimed capital, had been changed forever. More recently, such claims have increasingly been questioned, even dismissed as overblown clichés. Certainly, the mass exodus from New York that some predicted a year ago did not happen. A few Manhattanites fled to suburban safety, but most stayed.

The city's boosters claim that people were bonded more closely than ever to the Big Apple by the communal pulling together of the recovery effort. It is debatable whether this would have happened if the

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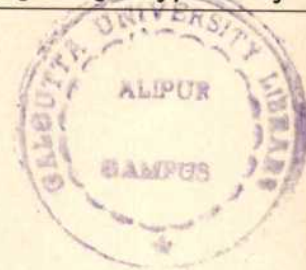
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terrorists had struck again, or had done so more effectively than with the few anthrax-carrying letters that were received last October from still-unknown authors. For now, the lure of New York has persuaded most of its inhabitants to gamble that September 11th was a one-off.

A second attack could dramatically alter such calculations for all Americans (see Lexington). But New Yorkers are understandably more nervous than most other Americans. In June, a Gallup poll showed that 19% of New Yorkers were very worried that they or a family member would become a victim of a terrorist attack in America, and another 34% were somewhat worried. This compares with 8% and 31% nationally (and the latter figures include two other cities recently hit by terrorism, Washington, DC, and Oklahoma City). Only 12% of New Yorkers said they now felt safe, down from 42% before September 11th.

A new CBS/*New York Times* poll suggests that fear of terrorism has eased a little in recent months. Even so, only 33% of the New Yorkers asked in the new poll expect their city to be a better place in the next 10-15 years, down from 54% a year ago. Only 57% of them want to be living in New York in four years; a year ago, the proportion was 67%.

This pessimism partly reflects the city's economic difficulties. New York's businesses have mostly stayed put—at least, those that have been able to stay afloat. Some public money went to aid firms in the vicinity of the World Trade Centre, especially small ones that catered to those who worked there—but that was not always sufficient to keep them going. All the same, much of New York's recession, which started in early 2001, is due to national and global problems that have had little to do with the terrorist attacks. Both ►►



► Wall Street and Madison Avenue were in trouble before September 11th.

This makes any estimates of the job losses associated with September 11th highly speculative. The city's unemployment rate rose to 7.7% in July, up from 6.3% in August 2001. The national rate jumped from 4.9% to 5.9% during the same period. Around 83,000 jobs disappeared from the city, and a further 63,000 that would have been created were not, because of the attack, according to a recent report issued by William Thompson, the city's comptroller. This report put the total cost to the city of the attacks at a massive \$83-95 billion, after accounting for every conceivable loss from higher borrowing costs to ruined property.

Such calculations surely overstate the terrorist impact, because they assume that the attack stopped a nascent economic upturn in its tracks. That gives insufficient weight to the damage that Wall Street would have suffered anyway due to the crisis of investor confidence following the collapse of Enron, the accounting scandals and so forth.

Those who stay away

The industry that was most clearly hit by September 11th was tourism. The occupancy rate at the city's hotels plunged to a miserable 62% last September (from 89% in September 2000), and their revenues fell to \$246m (compared with \$448m). Yet the situation has been improving steadily since then.

By June, the occupancy rate had risen to 78%, roughly the same level as the previous year, albeit with lower prices. Revenues for Broadway shows, which plunged in the last four months of 2001, were actually higher in May 2002 than in the same month last year. Air travel to New York is also rebounding, though it remains significantly lower than it was before the terrorists struck. And there has been a signifi-

cant shift in the mix of tourists visiting the city, with a rising number of American travellers partially filling the gap left by typically higher-spending foreigners who are staying away, especially the Japanese.

All the same, there is no doubt that New York (for whatever reasons) is worse off than it was this time last year. The result is that the city faces a looming budget crisis, with a likely deficit of at least \$2 billion next year that will be solved only by some combination of higher taxes and cuts in services. This year, hard budget decisions were postponed by using the September 11th attack to justify borrowing \$1.5 billion to cover the city's operating expenditures. This trick surely cannot be pulled off twice.

Steve Malanga of the Manhattan Institute, a rightish think-tank, is also pessimistic about renewed attempts, led by Senators Hillary Clinton and Charles Schumer, to get more federal aid for the city, including some to ease its budget woes. Congress has already given more than the \$20 billion initially pledged by George Bush to clean up the World Trade Centre. But politicians from other states are unlikely to see why the federal government should help with the general expenses of what is the biggest-spending city in America.

The task of solving the budget crisis will fall to Mayor Michael Bloomberg. The billionaire businessman is usually seen as one of the post-September 11th winners (if such a word can be so used): he would probably have lost the mayoralty to Mark Green, a leftist Democrat, had the terrorist strike not happened. Yet it is also worth noting that his election probably spared New York city a turbulent period of score-settling over Rudy Giuliani's legacy.

During his eight-year reign, Mr Giuliani bullied through a wide range of reforms, most conspicuously in policing. But the sheer scale of his assault, coupled with a personality of Thatcherite bluntness,

created a backlash. Mr Giuliani's critics, of whom Mr Green was one of the loudest, were silenced by his heroic leadership of the city after September 11th. Then Mr Giuliani's endorsement of Mr Bloomberg clinched his narrow victory.

Under Mr Bloomberg, a decidedly less ideological figure than either Mr Green or Mr Giuliani, the reforms have continued, with a few pragmatic twists. The crime rate is still going down. The mayor has been able to secure personal control of the city's schools. The current need to rebuild the city, and the public's recognition that finances are tight, have also taken some of the partisanship out of City Hall politics. Hopes even remain high that agreeing on a plan for what to do with Ground Zero will proceed without too much rancour, despite the lukewarm reaction to the first set of proposals unveiled in July.

A sweeter Apple

Behind this lies a conclusion that sounds trite and is impossible to prove: New York has become a nicer place. New Yorkers proclaim this frequently. But the city's impressive reaction to the attack has endeared it to the rest of the American people, many of whom had come during the previous half-century to regard New York as a godforsaken un-American place.

The ceremonial meeting of Congress in New York on September 6th symbolised this change in the city's status. Meanwhile, the public's spontaneous applause and cheers for the visiting Washington politicians showed that New Yorkers welcomed it. Ironically, through the loss of its tallest buildings, the city has resumed its traditional role, well described by E.B. White in "Here is New York", his classic 1949 essay: "It is to the nation what the white church spire is to the village—the visible symbol of aspiration and faith, the white plume saying that the way is up." ■

Iraq and the UN

Mr Bush lays out his case

WASHINGTON

The president's speech at the UN has pushed the stakes over Iraq even higher

IRAQ is "a grave and gathering danger", George Bush told the General Assembly of the United Nations on September 12th—not just to the United States but to the world. In a powerful and well-judged speech, the president called on governments everywhere to recognise that fact, and challenged the UN to respond to Iraq's "flagrant violations" of resolution after resolution. Mr Bush demanded no specific steps, proposed no timetables. He made it clear that America, in the end, would act alone against Iraq if need be. But he also made it plain that America would rather move in concert with others. He praised the UN, then called on it to live up to its responsibilities. His speech aimed to shift the burden of proof—and in some measure did so. In the face of the Iraqi government's crimes, he asked, how can the UN justify failing to act?

It had been a week of mounting pressure on Iraq. Over the weekend, Mr Bush met his closest ally, Tony Blair, for what was called a "war summit". On September 11th, in his address to the American people, Mr Bush, the Statue of Liberty glistening behind him, reiterated his determination to separate "tyrants" from weapons of mass destruction. On the same day, the Pentagon said it was sending 600 staff from its Central Command in Florida to the Gulf, ostensibly for a temporary exercise, but with everybody dropping hints that the generals would stay there longer to deal with Mr Hussein.

Mr Bush's speech to the UN also came against a background of tougher talk from some European allies, who had been widely assumed to be unwilling to face up to Mr Hussein. Last week, European foreign ministers demanded that Iraq let the inspectors back in, or else. This week, Jacques Chirac explained what this might mean. One UN resolution, said the French president, should give Mr Hussein three weeks to admit the inspectors. If Mr Hussein refused to comply, the world would have to consider a second resolution on whether there should or should not be an intervention. The wording would be crucial to France's own position.

That was woolly, but it did add to hopes that intrusive weapons inspectors, not war, might be the next step. Speaking before Mr Bush, the UN's secretary-general, Kofi Annan struck a similar note. He argued that "there was no substitute for the unique legitimacy provided by the

UN." But he also insisted that "if Iraq's defiance continues, the Security Council must face its responsibilities."

If Iraq accepted a completely uninhibited inspections regime, and complied in all respects with the demands the UN has already placed upon it, would that avert war? Without saying so explicitly, the president implied that it would. His insistence on "regime change" was somewhat tempered: he talked instead of the "prospect" of a new and different kind of government, at some unspecified point after Iraq had decided to behave. This part of the speech sounded more like Colin Powell than Dick Cheney or Donald Rumsfeld, who are known to regard inspections as useless, or worse.

At the moment, UN Resolution 1284 constitutes a standing offer to Mr Hussein: if the Iraqi government manages to satisfy the inspectors in every respect and co-operates in setting up a monitoring system, then sanctions could be swiftly suspended. Messrs Cheney and Rumsfeld still fear Mr Hussein would be able to run rings round such a regime, as he has before.

Several outsiders had argued that if Mr Bush went to the UN and proposed a new inspection regime with *carte blanche* powers of search and with military personnel on hand to help, it might have been accepted by the rest of the Security Council. He has not yet done that, in so many words. Instead, he produced his long and devastating list of Iraq's transgressions—and said that America would work with the Security Council to give Iraq one last chance. But the president warned sternly that "the purpose of the United States should not be doubted."

In a sense, Mr Bush has put the onus for designing a new resolution and making the inspections work on to the UN. If the Security Council proposes a tough regime, and if Mr Hussein accepts it, so much the better. Yet there are risks in America asking others to make the next move.

In the 1990s, Warren Christopher, Bill Clinton's secretary of state, was similarly frustrated by European reluctance to confront Slobodan Milosevic over Serb actions in Bosnia, and also said that he would wait while the Europeans sorted out what they wanted to do. The result was disagreement within NATO ranks while Serbs committed atrocities.

A policy of delegation risks getting America the worst of both worlds. If the other members of the Security Council propose having one more try at implementing the existing weapons-inspections regime, and if Mr Hussein accepts it (only to prevaricate again), Mr Bush would face an unenviable choice. He would either have to accept an inspections regime he disliked, or choose to disregard the very procedure he had just invoked and attack Iraq regardless. ■

West-coast ports

Slinging their hooks

LOS ANGELES AND SAN FRANCISCO

The west-coast dockers are blue-collar royalty. Will they be dethroned?

GOODS worth \$300 billion flow in and out of west-coast ports each year, \$220 billion of them through the giant terminals at Los Angeles-Long Beach. All this is loaded and unloaded by 10,500 dockers who belong to the International Longshore and Warehouse Union (ILWU). On July 1st, the contract between these dockers and the Pacific Maritime Association (PMA), which represents the shipping lines, expired. Until September 1st, the contract was extended one day at a time. Since then work has proceeded without any formal contract.

So far the cargoes have kept moving, with the work going on under the old terms, but a new contract needs to be negotiated. Any stoppage would hammer the economies of both America and Asia.

The ILWU has tremendous power not only over the PMA, but also over a swathe of American businesses, from retailers to manufacturers. The threat of a strike has long helped the union maintain high wages and unrivalled benefits. But the balance of power is changing. The shipping lines and their customers are better organised this time. And the White House, with one eye on the economy and the other on national security, has implied that it would intervene to prevent a stoppage.

The ILWU is rallying political forces of its own. All the west-coast senators have asked George Bush not to intervene. In London, the International Transport Workers' Federation is demanding that dockers in other countries support the ILWU if it is prevented from striking.

The underlying issue is technological change. The PMA and the rest of the sup- ➤



Ermine-collar work

ply-chain want the ports to operate more efficiently. Most big ports around the world use scanners and electronic data-transfer to speed containers through the docks, but on the west coast clerks still copy numbers down by hand and type them back into computers. West-coast ports also operate only eight hours a day; the other big ports work round the clock.

The union does not object to new technology. In the 1960s, it collaborated in the revolutionary introduction of containers, recognising that gains in efficiency could make up for lost jobs by raising the volume of trade. It was right: the amount of goods going through the ports has quintupled since 1980, and union membership, which fell from 16,000 in 1965 to 6,500 in 1983, has since climbed back to 10,500. But the ILWU frets that if data-processing replaces waterfront clerical work, it will lose control of it and, eventually, lose power.

The dockers are facing a challenge common to many other American unions. Structural change, away from manufacturing and towards services, has contributed to a drop in union membership from 22m in 1980 to 16m today. Even in its manufacturing heartland, barely one in seven American workers belong to a union.

A question of power

For the ILWU, the movement of jobs away from the waterfront and into a computerised back office, perhaps in another state, strikes at the heart of its culture. Union solidarity is hatched in the "hiring hall" to which workers report each day. Terminal operators hate the system: it delays the arrival of workers on the job in the morning, and since workers may be sent to a different terminal every day, it means that they do not build up loyalty to the firm that actually pays their wages.

Shipping lines share the blame for inefficiency, however. Each of the 14 different Los Angeles container terminals uses a different computer system, so a worker must spend time relearning what to do. Shipping lines justify the difference as a source of competitive advantage, but in practice it slows things down.

Even if the struggle between the global forces of trade and the practicalities of the waterfront remains locked, other pressures will soon force change. Gray Davis, the governor of California, is preparing to sign a bill—pushed by an unlikely alliance of frustrated truck-drivers and environmentalists—that would fine the operators of terminals that keep lorries waiting to pick up containers. Complying will mean giving drivers fixed appointments—and that will require better management of information. So, too, will federal anti-terrorism laws requiring identification cards for all transport workers. Whatever happens, data-processing is coming to the docks, and dockers will have to get used to it. ■

The mid-term elections

Politics goes on

WASHINGTON, DC

And the Democrats have reason to be pleased

SEPTEMBER 10th was not just a prelude to September 11th. It was also the second-most-important day in this year's electoral calendar: the day when 12 states and the District of Columbia completed the process of choosing their candidates for the November mid-term elections.

The primaries were dominated by a spirit of pragmatism. Across the country, party establishments did their utmost to make sure that their most electable candidates won the nomination. This meant eschewing ideological firebrands for sensible-looking people with a track record of solving problems.

The obvious reason for this is that America is a 50-50 nation: from Congress down to the state houses, the parties are evenly balanced. The Republicans are one seat away from taking control of the Senate. The Democrats are six seats away from taking control of the House. If the Democrats can win the governorship of a pivotal state such as Florida, they increase their chances of retaking the presidency in 2004. Nor is America in an ideological mood: the combination of the war on terrorism and the weak economy is predisposing people to look for pragmatic solutions to pressing problems.

Party establishments do not always get their way. In March, the White House failed to persuade California's Republican Party to choose Richard Riordan, the middle-of-the-road former mayor of Los Angeles, over Bill Simon, an untried ideologue. (Mr Simon has been flailing ever since.) But September 10th saw the establishment

winning across the board.

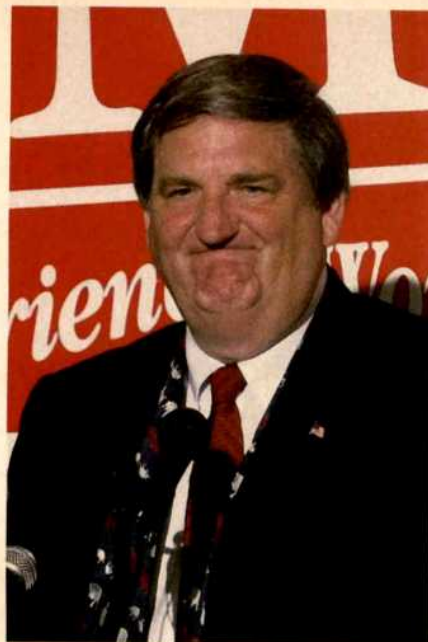
In the New Hampshire Senate race, Bob Smith, the state's Republican senator, lost to John Sununu, a congressman. Mr Smith had infuriated the party's establishment with his hardline conservative politics and idiosyncratic behaviour. He mounted a risible run for the White House in 1999; loudly quit the Republican Party to continue his run as an independent; and then rejoined the party just in time to assume the chairmanship of an important committee. Mr Sununu, on the other hand, is a solid party man, the son of a former governor and White House chief of staff in the first Bush administration.

In the Florida governor's race, Janet Reno, a former attorney-general, seems to have lost by a whisker to Bill McBride. After another fuss about voting machines (see box on next page) the election had not been certified when *The Economist* went to press, but Mr McBride had a lead of around 10,000 votes. Ms Reno started off as the front-runner, thanks to her celebrity status and strong support among blacks and the elderly. She tried to keep her popularity alive by driving around the state in a red pickup truck and hosting a "Janet Reno Dance Party" in a South Beach club. Mr McBride, by contrast, was an unknown first-time candidate.

But the party establishment never warmed to Ms Reno. They regarded her as too liberal, too idiosyncratic, too scarred by her role in the Clinton administration, particularly in the deportation of young Elian Gonzalez back to Cuba, to stand a se- ➤



McBride thinks he's won



Smith knows he's lost

rious chance of unseating Jeb Bush. Mr McBride, a decorated Vietnam-war veteran, won the endorsements of the Florida teachers' union, the state AFL-CIO and a slew of newspapers, besides using his financial advantage over Ms Reno to air expensive television ads.

In the North Carolina Senate race, Erskine Bowles, Bill Clinton's former chief of staff, beat off a grass-roots challenge by Dan Blue, a black state representative, to face Elizabeth Dole in November. In Maryland, Christopher van Hollen, the local party's favourite, came from behind to defeat a member of the Kennedy dynasty, Mark Shriver, in another example of Camelot's fading charms. It looks almost certain that Anthony Williams will defeat a challenge from Willie Wilson, a clergyman and associate of Marion Barry, and keep his job as the capital's mayor.

This year's primaries saw the development of a new political technique: picking your opponent. Gary South, Gray Davis's political guru, pioneered this technique by airing advertisements during the Republican primary demonising Mr Riordan, the candidate the Democrats most feared. Florida Republicans ran attack ads against Mr McBride. North Carolina Democrats tried to smear Mrs Dole for her association with Ken Lay, the disgraced ex-boss of Enron. In New Hampshire, where over a third of the voters are independent, Democrats may have crossed over to vote for Mr Smith. But the technique does not seem to have travelled well outside California: indeed, Mr McBride used the fact that the Republicans were trying to demonise him as evidence that he was a better candidate than Ms Reno.

These primaries have set the stage for a number of very close races in November.

Florida's new voting machines

If you really want to screw things up

MIAMI

Install computers and skimp on the training

AFTER Florida's disastrous presidential election two years ago, state officials were given \$32m to update voting equipment at polling stations. But the state still couldn't get it right. Instead of "hanging chads" and ambiguous ballot-papers, this time it was spanking-new computerised voting machines that caused all the grief. As the overseeing secretary of state (a man called Jim Smith, sadly no longer the fragrant Katherine Harris) put it, "What the hell have they been doing for the past two years?"

The biggest snafus were in the same three South Florida counties—Miami-Dade, Broward and Palm Beach—where most of the problems occurred in 2000. In Miami-Dade, many of the county's 754 polling stations opened late. A few were not up and running until the afternoon, more than five hours after they were meant to be. Thousands of voters had to be turned away, and not all could come back later. Governor Jeb Bush, calling the mess "shameful", declared a state of emergency to force the polls to stay open two more hours, until 9pm.

In some cases, poll workers simply

failed to turn up. Where they did, they often did not know what to do with the shiny gizmos in front of them. The new touch-screen system requires voting machines to be booted up with a cartridge before they can be used, a process that takes about six minutes. In their haste, some workers pulled out the cartridges too soon, crashing the machines.

Officials waited too late to train poll workers on the new equipment. In Miami-Dade and Broward some poll workers, mostly elderly people unfamiliar with computer technology, didn't like the newfangled system and dropped out of classes. Election officials scrambled to replace them.

All this could well have affected the outcome of the Democratic primary between Janet Reno, a former attorney-general, and Bill McBride. South Florida's three counties have by far the biggest number of voters. Their large black and Jewish populations are Ms Reno's stronghold, where she out-poll her rival Mr McBride by a margin of more than two to one.

Yet voters were unable to cast ballots until nearly mid-day at one Miami precinct, Jordan Grove Missionary Baptist Church in Liberty City, a poor black neighbourhood that is strongly pro-Reno. All the poll workers had been to their classes, but the machines would not boot up properly. "We turned away about 450 people. It was a huge turnout," said Pam O'Riley, a Reno campaign worker, standing outside in the rain. "I was in tears at one point. This will definitely hurt her campaign." Whatever the final result, the recriminations will continue. The next test will be the election in November.



Oh, Florida

Most are good news for the Democrats. Erskine Bowles could make Mrs Dole's life difficult. He has made a small fortune as an investment banker, and he comes from one of the most prominent political families in the state. His pragmatic style and business background should go down well with whites, while his connections with the Clinton administration could bring in the black vote.

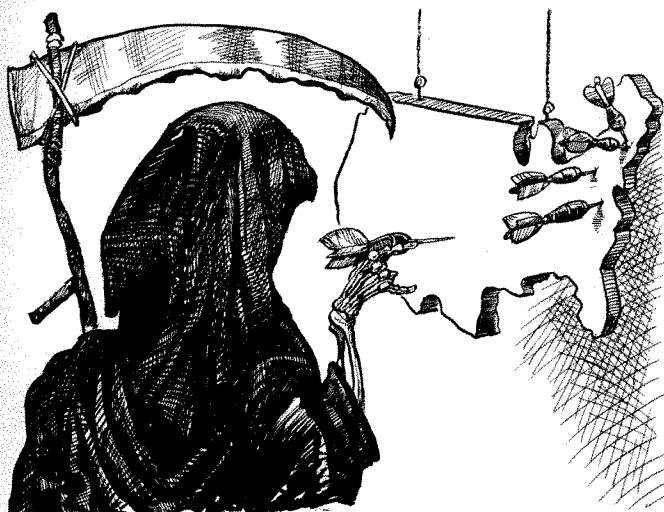
Mr McBride also has a chance of beating the president's brother. Mr Bush has been dogged by well-publicised problems with the state's Department of Children and Families, which has a habit of misplacing children in its care, and with his own daughter, who was caught in posses-

sion of cocaine this week. The fact that the governor has evidently failed to keep his promise to improve the state's voting machinery may also cost him votes after this week's debacle.

The Republicans received more bad news from New York, albeit of an eccentric sort. It looks as if Thomas Golisano, a multi-millionaire who wants to spend pots of money trying to take the governorship away from George Pataki, has secured a place on the November ballot as the Independence Party candidate. The Republicans will now be forced to spend valuable time and treasure trying to defend two governorships, Florida and New York, that until recently looked like shoo-ins. ■

Lexington A ghastly probability

A second terrorist attack would probably change America even more than the first one did



THERE is never a good time to contemplate the possible murder of more Americans. As the country pauses to mourn the dead in New York, Washington and Pennsylvania, now may seem more than usually inapposite. It may also be necessary.

September 11th 2001 was an all-consuming moment. It saw the most grievous one-day massacre in America since the civil war. It is not surprising the anniversary commemorations have grabbed so much attention. But the character of the observance is revealing. Despite the fresh round of warnings this week about the possibility of another attack, many Americans—perhaps most—still seem to treat the attacks as if they were a single, dreadful event, like a natural disaster, or a random crime committed against America, with the Bush administration meting out punishment, most of it abroad.

Yet the destruction of the World Trade Centre was not a one-off event. Al-Qaeda attacked America four times in the past decade, bombing the World Trade Centre for the first time, the Khobar towers in Saudi Arabia, two East African embassies and the USS Cole. Last year's atrocity was different in scale, not in kind. It was a fifth attack. Since then, al-Qaeda has been badly wounded, but it has certainly not been destroyed. It has committed some subsequent acts of terror, and failed to carry out more. Members of its inner circle are said to be regrouping in Iran, Afghanistan and elsewhere.

Now imagine how Americans might react if these al-Qaeda remnants resumed operations—if, say, the prime minister of Afghanistan were assassinated, or if hundreds of American soldiers were killed at a base in Germany. These events are not hard to imagine: both came within a whisker of occurring recently. But the biggest psychological impact would come from an attack on the United States itself—and here the possibilities remain frightening, because they need not be as sophisticated as the last attack. It would not be hard, for instance, for 10 suicide bombers to attack malls around the country.

Yet America seems unwilling to indulge in such imaginings. Nobody took that much notice of this week's warnings (perhaps because there have been so many before). Turn-out in the primary elections fell a bit, though not sharply. The current attitude to future attacks seems to be nervous denial: people do not want to think about it. Even memories of the anthrax letters have

faded: these are not seen as part of a pattern of attacks because Americans do not think they had anything to do with al-Qaeda. All this stands in sharp contrast to the outpouring of grief over the mass murders of a year ago.

The difference is important. September 11th reminded Americans of things that make them special—exceptional patriotism, religiosity and willingness to use force abroad for moral reasons. But it did not fundamentally alter the way the country is run or how Americans think about themselves. Another attack would. The World Trade Centre would more clearly become what George Bush has long insisted that it was: an act of war.

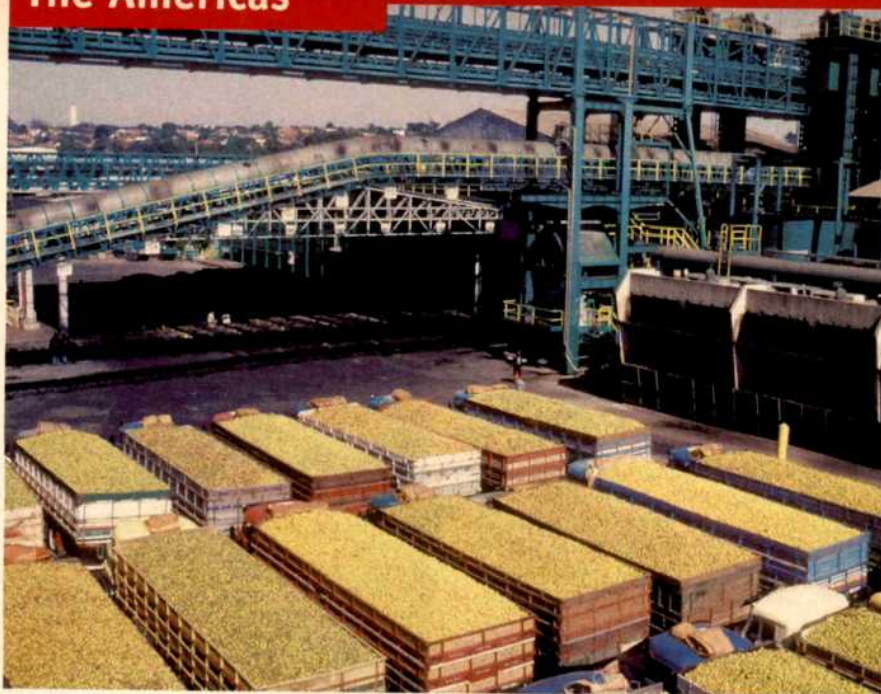
And war is different. In war, the long conflict itself is what matters. Individual atrocities—even one as big as September 11th—become secondary, important not so much in themselves but for what they tell you about the wider struggle. Wars, including long-drawn-out ones against terrorists, take on a momentum of their own.

Prepare yourself

So a second strike would surely change America more than the events of September 11th alone did. But how? The best hope would be that Americans would react rather as they did in 1941, with a great outward-looking surge of determination to root out terrorists in concert with their allies. The worst fear is the opposite: America could begin listening to the sirens of isolationism again. Some voices would surely be raised, complaining that the country gets nothing from the rest of the world and should retreat from it. These voices would surely not prevail. There is no popular support for isolationism now. And disengagement would be enormously costly, even impossible (because America's enemies are already inside the country).

The most likely reaction would be bloody-minded unilateralism—of the sort Mr Bush is often accused of now. Americans might well say, in effect, "We are being attacked. Not Europeans. Not Middle Easterners. Us. We consulted with you over Afghanistan and even Iraq. Now we will act as we see fit." Mr Bush's inner circle would surely become even more likely to disregard international treaties, even more likely to lash out against potential foes and even more defiantly pro-Israel than it already is. Some European and Arab allies might regard this as little better than outright isolationism. A bigger version of the existing gap would open up—with Mr Bush smiting his enemies and his allies whingeing about the underlying causes of terrorism.

A sobering possibility, and one that might yet be avoided. Look at the question of more terrorism another way: in the light of another attack, how would Mr Bush's current strategy be reassessed? The president's defence would be easy: all along, he has been treating the battle with al-Qaeda as a long-term war. All the same, if an assault happened next month, or next year, Mr Bush's critics would carp on about three things. First, he should have found more common ground with America's allies. If only he had been seen to be doing more to tackle those underlying grievances. Second, they will say that he should have built more bipartisan support at home for his social and fiscal policies. Lastly, they will argue that the president could have done more to prepare the country for war—not merely by issuing colour-coded warnings but by forgoing future tax cuts to finance an escalating struggle with terror. A fearful list, which Mr Bush will dismiss. But if he believes his own rhetoric, it is a political struggle he will have to prepare for. ■



Trade in the Americas

The geopolitics of orange juice

SAO PAULO

The battle for an Americas-wide free trade pact is hotting up. Its prospects depend in part on Brazil's election campaign

IT IS more than a decade now since President George Bush's father first floated the idea of a Free-Trade Area of the Americas (FTAA). Since 1998, negotiators from 34 countries have been quietly working to try and conclude such a pact, which their political leaders have agreed should come into force by January 2005. But although the idea has influential champions and bureaucratic momentum, it has never been clear whether the United States and Brazil, respectively the largest economies in North and South America, will end up throwing their full political weight behind the proposed FTAA. The next few months may settle that question.

Having seen how Mexico's exports have boomed under the 1994 North American Free-Trade Agreement, many other Latin American governments, faced with torpid economies, are desperate to get better access to the America market. But over the past year, relations between Latin America and the United States have been difficult. Despite Mr Bush's declarations of love for the region, the war on terrorism has imposed other priorities. The administration's seeming indifference to Argentina's economic collapse caused dismay in the region. Huge new subsidies for American farmers, and tariff protection for its steelmakers, enraged Brazil.

Recently, though, the United States has

performed several about-faces. Last month, Congress finally approved an omnibus trade bill, which grants the administration the "fast-track" authority needed to clinch trade deals (this means that legislators can reject but not amend them). Days earlier, the administration had proposed that the current round of World Trade Organisation (WTO) talks should agree to worldwide cuts in farm subsidies. And the United States' Treasury not only backed a \$30 billion IMF loan-package for Brazil but itself stumped up a \$1.5 billion bridging loan for Uruguay.

American officials express optimism that the FTAA talks will now move forward according to schedule. This calls for the United States and Brazil to take over the joint-chairmanship of the talks at a ministerial meeting in Quito, Ecuador's capital, on November 1st for the final, tough, phase of bargaining.

Hope and disquiet

But the FTAA prompts disquiet as well as hope. Robert Zoellick, the United States' Trade Representative, this week met his counterparts from the Caribbean, who are worried about their small countries' ability to compete. Venezuela's president, Hugo Chavez, a populist, is a critic of the plan: his government says it may hold a referendum on the FTAA next year.

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In Brazil, long more sceptical than many of its neighbours, the FTAA has become an issue in next month's presidential election. This month, Brazil's Catholic bishops organised a "plebiscite", inviting the public to express opposition to the proposed accord. Against, too, until recently were Luiz Inacio Lula da Silva, who leads the polls for the election, and his left-wing Workers' Party. But the prospect of power has softened their stance; they withdrew backing for the church's plebiscite. Mr da Silva still calls the FTAA an "attempt at annexing Latin America" by the United States. But though he is against it "as it is currently being negotiated", he says he might accept a deal that gave Brazil fair access to America's market. For his part, Jose Serra, the government candidate, whom polls place second, joins in the attacks on American protectionism while insisting he is best-placed to negotiate it away.

Many Brazilians blame freer trade for lost jobs: after opening up its economy in the early 1990s, Brazil suffered big trade deficits. Now, with a weak currency, the country is heading for a trade surplus of \$7 billion this year; similarly, Brazil's trade with the United States has moved from deficits to a likely surplus of around \$3.5 billion this year. The turnaround is mainly due to a fall in imports as the economy has slowed. Brazil urgently needs to boost exports, to grow while cutting its dependence on foreign financing.

But powerful interest groups are sceptical about the FTAA. Sao Paulo's industrialists' federation has published a study suggesting that the pact could lop \$2.2 billion a year off Brazil's trade surplus. Sergio Amaral, the trade minister, is sceptical of this and has commissioned fresh studies, due to be released later this month.

▶ An FTAA might settle some bitter trade rows between Brazil and the United States. Brazil has filed a complaint to the WTO over the new steel duties (though its exports were exempted from most of these). As well as high tariffs, Brazil's orange juice (it is the world's biggest producer) faces a surcharge levied by the American state of Florida—the subject of another complaint at the WTO. Brazil may also challenge America's subsidies to its cotton farmers at the WTO. And it complains about high American tariffs on its exports of sugar, textiles, tobacco and ethanol.

Some Brazilians argue that the WTO is a better forum than the FTAA in which to achieve free trade. Brazil has repeatedly said that an FTAA must encompass farm subsidies and "anti-dumping" measures, but American officials say they will negotiate these only at the WTO talks (which are likely to drag on beyond their 2005 deadline). Brazil had once hoped to head a powerful block at the FTAA talks, centred on Mercosur. But Argentina's collapse has turned Mercosur into a shell. And that has taken the urgency out of free-trade talks between the European Union and Mercosur (also supposed to finish in 2005).

Meanwhile, the United States is close to completing a bilateral trade deal with Chile. The omnibus trade act also extended duty-free access for farm (and now textile) exports from the Andean countries (except Venezuela), seen as alternatives to illegal drug production. This all adds to Brazil's relative isolation in the FTAA talks.

American officials insist that such deals are a way of building momentum towards the FTAA. They, too, face doubters at home, and have their own wish-lists. A meeting in New Mexico of American sugar farmers in early August heard a presentation entitled: "Brazil: Poised to Swamp All of US Agriculture". The United States insists that government procurement should be covered by the FTAA, something which Mr da Silva might object to. He says he would reverse a recent decision by Petrobras, the state oil company, to buy drilling platforms from Singapore. He argues that government business should be used to create jobs in Brazil.

Despite such public slanging, progress has quietly been made in preparing the final stages of the talks, says Jeffrey Schott of the Institute for International Economics, a Washington think-tank. The chances of success will become clear only by mid-2003, when all the countries have put their offers on the table. Brazil and the United States each expect sweeping concessions from the other. Both will also be tied up with the WTO talks, and Brazil with those with the EU too. With so much bargaining to be done, the timetable may slip, and a deal might not come till 2006. But slow though the process is, it still shows stubborn signs of life. ■

Healthcare in Chile

A new prescription

SANTIAGO

A minimum plan for sickness—and health

SINCE last month, children with cancer and adults with heart disease or kidney failure have enjoyed the right to be treated within a specified time in Chile's hospitals. By 2004, another 53 diseases should have been added to this list, as part of a big shake-up in health care launched by President Ricardo Lagos's centre-left government. The aim is to tackle the unfairness and inefficiencies that besmirch one of Latin America's better health systems.

On basic health indicators, Chile scores well. Infant and maternal mortality are among the lowest in Latin America. Average life expectancy is almost 76 years, up from just over 60 years in the early 1970s. But the average conceals glaring inequality. Infant mortality in a poor rural community of southern Chile is four times the national average and sixteen times that of a prosperous Santiago suburb, according to a recent study. That mirrors unequal income distribution. But it is also a result of changes introduced by General Augusto Pinochet's dictatorship of 1973-90.

All Chileans with jobs pay at least 7% of their salary to health-insurance providers. Since the dictatorship, those who wish (1m, or 20%, do) can pay this not to FONASA, the public health-insurance fund, but to private funds known as Isapres. These offer swift access to well-equipped private clinics—for a price. The average contribution to an Isapre is 9% of (above-average) salaries. Even so, members pay out a similar amount on top of their contribution for off-plan items and prescription drugs, according to the government. FONASA, which is topped up with a public subsidy, buys care at (dowdier) private clinics as well as public hospitals.

Since 1990, democratic governments have thrown more money—three times more—at the public system, but without reforming it. Waiting lists are long. Public hospitals, which must offer free care to the poor, are overstretched, after years of past underinvestment. But they are also grossly inefficient. Even General Pinochet quailed at taking on medical unions. So hospitals cannot sack specialists, even when they have too many of them and too few of others; doctors with more than 20 years service work short hours.

The reform centres on the new minimum-care plan, offering guaranteed free or low-cost treatment for 56 ailments that between them are responsible for three-quarters of years of life lost because of pre-



Breathe in and pay up

mature death or disablement. This plan, which both the public and private systems would have to offer, would be paid for from a new national fund, into which wage-earners would pay part of their contribution. The Isapres would no longer be able to charge more to elderly patients, at least for the minimum plan. Hernan Sandoval, the reform's author, says he hopes that these changes will direct resources where they are most needed, while encouraging patients to demand their rights.

The reform is popular with the public—but not with health workers. Doctors see standardised treatment as a first step towards managed care and, therefore, as a threat to their incomes. Public sector health-workers worry that job security could be at risk. The Isapres are wary, but see some advantages. The new system would give them greater control over who provides treatment, and therefore over costs, without impinging on their freedom to offer top-up coverage.

But the biggest sticking point may be opposition in Congress to the tax increases required to pay for the reform. The government says the reform will add an extra \$230m to Chile's total spending on health of \$4.3 billion (or 6% of GDP). Most of the extra money would come from the public purse. So it is not clear whether the government will get its way. If it does, it might just make Chile's health system fairer and more efficient—but at a cost. ■

Gambling in Canada

Hard luck story

MONTREAL

Losing their heads over lotto

CANADIANS like to think of themselves as prudent, level-headed, people. Yet that self-image is a little out of date. In less than a decade, the amount they lose in lotteries, casinos, slot machines and the like has quadrupled. The average Canadian now admits to spending C\$424 (\$270) per year gambling. Since most people lie to themselves about such matters, the true figure may be as much as C\$1,000.

Only a generation ago, charity bingos and church raffles were about as risky as things got. Now there are 60-odd casinos scattered across the country; many are in Indian reservations, where they are valued for jobs as well as revenue. Daily lotteries often pay out C\$10m or more. Video-lottery machines, dubbed gambling's crack-cocaine for their cheap, fleeting thrill, are particularly popular. Staff in corner shops now regularly ask customers whether they want a lotto (loto in French-speaking Canada) with their shopping.

All of this is manna for Canada's provincial governments, who are the monopoly owners of legal gambling outlets. These provided profits totalling C\$6 billion in 2001. In Alberta, the richest province thanks to its oil and gas, gambling may soon overtake corporate income tax as a source of revenue.

Perhaps that is why governments have seemed reluctant to consider gambling's social impact. "They don't ask the questions they don't want to know the answers to," says Jason Azmier of Canada West Foundation, a Calgary-based thinktank which recently concluded a three-year study of gambling.

But some are starting to ask questions—or at least to look for others to blame for their own stupidity. Loto-Quebec, the agency that runs gaming in the province, is being sued for almost C\$700m on behalf of an estimated 125,000 pathological gamblers. This class-action suit is led by Jean Brochu, a lawyer from Quebec city, who embezzled C\$50,000 from his professional body to feed into video-lottery terminals. It is backed by another government agency, the coroner's office, which blames gambling for 71 suicides in the province between 1999 and 2001.

More predictably, churches also rail against government's embrace of gambling. They argue that Canadian Indians are the most hurt by the casinos on their reservations. Pathological gambling is ten times more common among Indian peo-

Mexico city

Centre of belated attention

MEXICO CITY

An effort to revive a historic slum

THE huge square known as the Zocalo is no longer the beating heart of Mexico city, as it was in Aztec times. But it is surrounded not just by a magnificent cathedral but by nine square kms (3.5 square miles) of Spanish-colonial houses, churches and public buildings, some dating back to the 16th century. This should be one of the most compelling architectural destinations in the Americas. Instead, much of it is a slum of gutted buildings, dark and dirty streets blocked by milling vendors, and garbage-strewn vacant lots.

The reasons for this sad decline are partly man-made, and partly natural. In the 1940s, the city government froze rents in the city centre. Tenants paying 50 cents a week in 1950 were still paying the same in 1998, when the law was finally repealed. With no incentive to

spend on upkeep, landlords let buildings disintegrate. A 1985 earthquake added to the Beirut look. The result: 100,000 city-centre residents, over a third of the total, have moved out in the past 20 years. By night, the area is almost deserted; fear of crime deters most visitors.

For a decade, attempts have been under way to rectify matters. Carlos Slim, Mexico's richest businessman, has bought up and renovated some of the old buildings to prevent their collapse. Now the city government has started to do its bit. Last February, it revamped the Historic Centre Trust, a quango, endowing it with a grant of 500m pesos (\$55m).

The trust has begun work on renovating the 34 blocks in the heart of the historic centre, behind the cathedral. The streets are being dug up to replace the antiquated drainage system and to improve water supply. In an innovative move, an architect has been put in charge of each of the 13 main streets, charged with restoring the facades of more than 500 buildings. The makeovers have been designed in consultation with residents. Last week, Andres Manuel Lopez Obrador, the city's left-wing mayor, also announced the start of work on a new square.

Further ahead, the plan is to move the street vendors out of the area, says Ana Lilia Cepeda, the head of the Historic Centre Trust. That will be difficult: many of them bribe local officials to be there. The overall aim is to attract new residents to the centre, and with them cafés and restaurants—and a feeling of safety in numbers. If the promised street lighting, video cameras and the paraphernalia of modern urban security duly materialise, such gentrification may indeed follow. After all, surely somebody will want to live in some of Latin America's grandest housing.



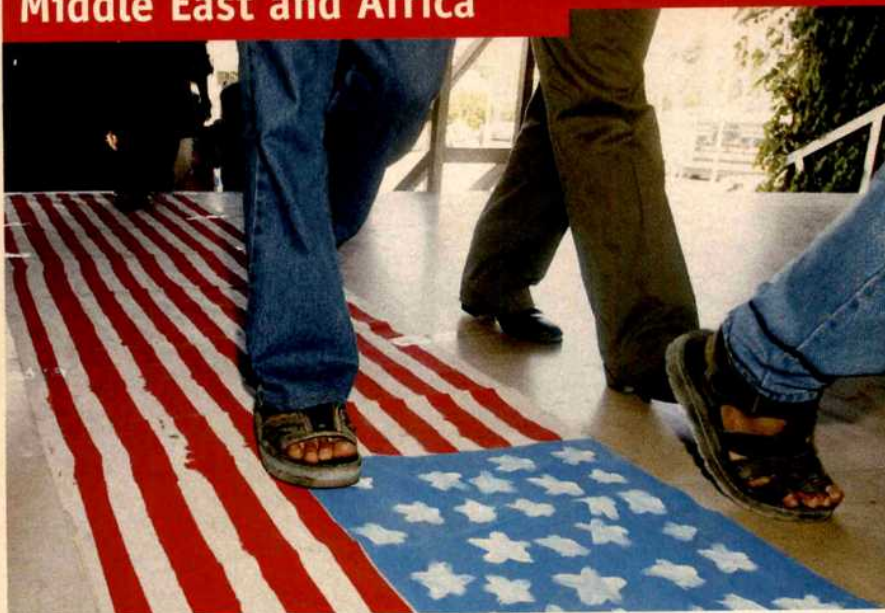
Estate agent plumbs new depths

ples than other Canadians. On and off the reserves, gambling brings child poverty, stress, marital breakdown and crime, say its critics. They include John Ralston Saul, a writer and the husband of Canada's governor-general, who has denounced "the state funding the public good by corrupting the citizen".

But Canadians seem unmoved by these pleas to be protected from themselves. Canada West Foundation found that they placed gambling behind highway speeding in the hierarchy of social ills. Faced with a choice between more gam-

bling or higher taxes, more than three times as many plump for the first.

Mr Azmier reckons Canada has up to 1m problem-gamblers, but they are invisible. "It doesn't make you stumble. You don't slur your speech. It can't be smelled on your breath," he says. As a result, Canadians are unaware of the social cost of government's profitable love affair with gambling. Even if some provinces have made gestures aimed at slowing the industry's growth, the amount transferred each year from the pockets of citizens to government coffers is set to keep on climbing. ■



Arabs and America

In America we do not trust

CAIRO

Arabs intensely dislike American policy. But this doesn't mean they will defy it

AMERICANS think we should be more like them, goes a bitter joke currently consoling Arabs, but every day they look more like us. They have a hereditary presidency, corruption, terrorism, Israeli-occupied territory (Capitol Hill), and a bad record for human rights. Now they want to do to Iraq what Iraq did to Kuwait.

What people find funny is often revealing. One thing this joke illustrates is that in the past year Arabs, even more than before, have come to regard American motives with scepticism (or outright incredulity), and American power with panic. Another is that Arabs have never felt their own failings so keenly.

Disenchantment with America is hardly an Arab monopoly. Yet the erosion of post-September goodwill has been particularly complete in a region that feels it is being condemned collectively for the sins of a few. The looming invasion of Iraq, and the sense that other Arab targets may be next, have further soured the mood.

In its mildest form the attitude is one of simple disappointment. Egypt's foreign minister, Ahmad Maher, laments that America lost a unique chance to rally the world to its side after last year's attacks. It lost the chance by applying the "with us or against us" judgment in pursuit of narrow interests rather than broader principles.

More commonly, Arabs are aggrieved by what they perceive as an American failure to listen to them. Why do they hate us?, Americans ask. They answer the question

by persuading themselves that the hostility of the "Arab street", a hostility that al-Qaeda carried to savage extremes, stems from some kind of cultural envy, made poisonous by the oppressiveness of Arab societies and states.

But, as any simple Arab citizen will confirm, resentment of the superpower has never been a response to America itself. Rather, it is a response to its policies: its throttling of Iraq, sanctioning of Libya and Sudan, and, above all, its generous bank-rolling of Israel. "Take Israel out of the equation," says a businessman in Jeddah, "and, poof, we've basically never had a problem with America."

To the dismay of America's friends in the Arab world, the perceived tilt against them has grown more extreme in the past year. Countries such as Syria and Yemen have bridled at accusations that they harbour terrorists, whatever the truth of the charges. The lumping of groups such as Hamas and Hizbullah into the same camp as al-Qaeda has jarred with the Arab view of them as freedom fighters, whose cause, if not always their methods, is legitimate.

Saudi Arabia has been mauled in the American press, and seen its peace initiative ignored. Racial profiling of Arabs by American authorities, and right-wing talk of mounting a "crusade", or "redrawing the regional map", and, spectacularly, the praising of Ariel Sharon as a "man of peace", have all ignited Arab alarm.

Instead of trying to douse extremism,

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says Raghida Dergham, who reports incisively from New York for a liberal daily, *Al Hayat*, the Bush administration has seemed intent on inflaming it. Her explanation is that American policy has, in effect, been hijacked by a coterie of officials whose obsession with Israeli interests has warped America's whole approach to the region.

Such is the view of a noted moderate, and one privately shared by most Arab governments. But the more popular view is that America is not just being manipulated by Israel, but that it has its own wicked agenda. "What America wants is to dismantle the Arab world," declared a speaker at a year-after forum in Cairo.

Damascus radio talks of plans to "recolonise" the region. Abdul Bari Atwan, editor of a radical Arab daily, *Al Quds al Arabi*, outlined a scenario whereby Israel would be made "the trusted sentry guarding the oil fields while the Arabs, or what remains of them, revert to rearing camels."

Such alarmism has triggered calls for a stronger diplomatic response. American bases in the Gulf should be closed, say some. Joint defence pacts should be invoked to protect Iraq, say others, and Arab money withdrawn from America. But while sporadic boycotts of American goods have broken out, the most that a recent gathering of foreign ministers from 20 Arab countries could muster was a resolution calling for "a complete rejection of threats of aggression against some Arab countries, in particular Iraq."

And that is about as far as official Arab opposition to "regime change" in Iraq is likely to go. Behind the scenes, many governments are signalling acquiescence in America's plans. This is partly in recognition of the limits of their power in the face of American determination. It also reflects frustration with the Iraqi regime, mainly because of its blind stubbornness. ➤

Arab visitors to Mr Hussein have been shocked to find that he really intends to fight, or so he says. In response, the tone of pro-government commentary in countries such as Egypt and Jordan has changed. Baghdad should understand that sympathy for the Iraqi people does not mean that their leadership is liked, or that other Arabs will fight America on its behalf, scolds Cairo's official daily, *Al-Ahram*. Jordan will not commit suicide for Saddam's sake, echoes a columnist in Amman.

Quietly, too, another undercurrent of thought is spreading. Arab governments may tremble at the thought that regime change may prove contagious, but a growing number of their citizens think it is maybe not such a bad idea. The exposure of Arab weakness has prompted unusually outspoken criticism, even in such police states as Syria and Saudi Arabia. The gist of the message is that if the Arabs want to be strong, their governments must devolve more power to the people. ■

Iraq

Defiance and death

BAGHDAD

September 11th, say Iraqis, became an excuse to persecute them ever more

SYMPATHY on the first anniversary of the terrorist attacks against New York and Washington was in low supply on the streets of Baghdad. September 11th, say ordinary Iraqis, provided the United States with an excuse to step up its persecution of the Iraqi people. They have come to accept that war with America is inevitable, but their response, at least as proclaimed to a group of journalists, was defiant. Some echoed the bravado of their foreign minister, Naji Sabri: "Even if it is with palm-tree sticks, we will fight back."

September 11th also made it easier, says Amer Muhammad Rashid, Iraq's oil minister, for the Americans and British on the UN sanctions committee to justify tightening the economic noose round Iraq. One result, he says, is the drop in oil sales over the past four months. This is partly due to the fear of war, but also the new restrictions imposed on the pricing mechanism (to avoid the payment of illegal kickbacks) which mean that buyers do not know until a month later the price at which they are buying Iraqi crude. Iraq now exports under 1m barrels a day through the UN, compared with 1.7m bpd last year.

Tighter rules on imports do visible damage. Six months ago, Ali Asiyan, a nine-year-old leukaemia patient, had a good chance of survival. Today he is very likely to die. This, says Luay Qusha, the

chief doctor at Baghdad's Al Mansour paediatric hospital, is because for the past six months the UN has not allowed Iraq to import radioactive agents used to diagnose and treat cancer on the grounds that they could be used to produce "dirty" bombs.

"I want my child to live but the Americans want all Iraqis to die," said Ali's mother, a gaunt woman swathed in a black chador. Emaciated children sit listlessly on their beds. In another ward are the prematurely born babies, their tiny bodies mangled with deformities. The UN's oil-for-food programme helps, "but only the tiniest bit," says the doctor, pointing to rows of empty medicine cabinets.

Dr Qusha says the high rate of cancer, premature births and birth defects is chiefly due to the exposure of their parents to radioactive materials left over from the 1991 Gulf war. Health Ministry statistics say that the incidence of abnormal births has increased 400-fold since 1991. The Iraqis also say that, all told, 1.7m children have died because of the various effects of UN sanctions. In the West, the Iraqi government is held to blame for contributing to and manipulating this tragedy.

At the Tuweitha nuclear facility just south of Baghdad, Iraqi scientists who produce chemical agents used for cancer treatment know that they will be among the first targets if the Americans and British launch an attack. They know this, they told correspondents, because the British released a map last week showing satellite images of Tuweitha to support the claim that the Iraqis have resumed producing nuclear materials at the plant.

There is little doubt that it did once. The plant's largest reactor was destroyed by Israeli bombers in 1981. American and British bombs smashed the two remaining reactors during the Gulf war. But since then, or so claim the Iraqis, the site has been clean, and was repeatedly searched by the UN inspectors until they left in 1998. ■



Radiotherapy is denied him

Iraq's arsenal

Perhaps

The IISS's assessment

☢ Nuclear/radiological

- Does not possess facilities to produce fissile material in sufficient amounts for nuclear weapons.
- Would require at least several years and extensive foreign assistance to build such fissile material production facilities.
- Could probably assemble nuclear weapons within months if fissile material from foreign sources were obtained.
- Current interest in radiological weapons unknown. Could divert domestic civil-use radio-isotopes or seek to obtain foreign material for a crude device.

☠ Biological

- Probably retained substantial growth media and agents from pre-1991 stocks.
- Capable of resuming agent production on short notice (weeks) from existing facilities; could have produced thousands of litres of anthrax, botulinum toxin and other agents since 1998. Actual stocks unknown.
- Production of viral agents, possession of smallpox unknown.

☪ Chemical

- Probably retained mustard and precursors for a few hundred tonnes of sarin/cyclosarin; perhaps similar amount of vx from pre-1991 stocks.
- Capable of resuming production on short notice (months) from existing civilian facilities; could have produced hundreds of tonnes of agent (mustard and nerve agents) since 1998. Actual stocks unknown.

✈ Delivery means

- Probably retained a small force of 650km (400 mile) range al-Hussein missiles, perhaps around 12 missiles.
- Lacks facilities to produce long-range missiles, would require several years and extensive foreign assistance to construct such facilities.
- May have produced some al-Samoud missiles, with ranges up to 200km.
- Capable of manufacturing rudimentary chemical and biological warheads.
- Capable of converting civilian vehicles to mobile launchers.
- Capable of delivering biological weapons with simple airborne wet-spray devices; development of more advanced devices for wet spray or dry agents unknown.

Source: The International Institute for Strategic Studies

Namibian land reform

Talking like Mugabe

WINDHOEK

But Namibia's Sam Nujoma is not as reckless as he sounds

IT ALL sounds worryingly familiar. Sam Nujoma, Namibia's grizzled old president, who has ruled since independence in 1990, last month berated "arrogant" commercial farmers for blocking land reform. He said, not unreasonably, that Namibians were angry that a few thousand white farmers still control 36m hectares (89m acres). This is 70% of the country's privately-owned land, and 44% of its total land mass.

He says that he wants to expropriate 192 farms, mostly owned by Germans and South Africans, and adds that unless the owners co-operate, Namibia will go the way of Zimbabwe. Last week, at the UN development summit in Johannesburg, Mr Nujoma emphasised his point by cheering Robert Mugabe, blaming Britain for Zimbabwe's woes and declaring, disingenuously, that Africa does not need western investment.

His words grabbed the headlines. But even though Mr Nujoma and Mr Mugabe are close allies, few expect Zimbabwean troubles in Namibia, or anyhow not just yet. Unlike Mr Mugabe, Mr Nujoma does not feel threatened by his feeble domestic opposition, so he does not need to use land reform as an excuse to crack heads. Diplomats in Windhoek argue that Mr Nujoma's frequent outbursts belie his government's moderate policies. He often rants against homosexuals, for example, but has done little to persecute them.

This week, Mr Nujoma's new prime minister, Theo-Ben Gurirab, said that the government would continue to acquire land for redistribution mainly from willing sellers. By law, it has first refusal on any farm for sale, and pays market prices. Although the process has so far led to the resettlement of only 100 farms, this is partly because of the difficulty and cost of teaching former cow-herders to manage enormous and sprawling ranchland effectively.

It will take time, and aid money for irrigation, roads and equipment, for any of these resettled farms to become self-sustaining. More may have to be done to support farmers once they have land, for example by granting cheap "affirmative action" loans to new black farmers.

The Namibian Agricultural Union (NAU) is not braced for great upheavals. Next year, the government plans to introduce a small tax on under-used farms, to encourage more farmers to sell plots. According to Gert Grobler of the NAU, Mr Nu-

joma's plan to expropriate farms will probably lead to the forced purchase of only "one or two" unproductive farms now owned by foreign, absentee landlords, and used as hunting grounds. As for Zimbabwean-style land invasions: "Forget it. Anyone who invaded a cattle ranch would soon die of thirst," he scoffs.

But some individual commercial farmers are more anxious. This week, over 150 of them gathered at a ranch in eastern Namibia for a sundown bull auction and party. Between mouthfuls of cake, they grumbled about official meddling, the failure of farms resettled by poor black workers, and the risks to investment whenever the "old man" shoots his mouth off. A Scottish speaker then explained how to use God's love to fend off land-invaders.

The farmers' greatest worry is that land reform is becoming a political issue. Elections are due in 2004. The popular Mr Nujoma has promised to step down, but

could always change his mind. If he does, he will have to convince his party to carry on backing him. Inequitable land distribution could give him an excuse to stay on, to finish the job of liberating Namibians from white domination.

In the meantime, he could do something useful in northern Namibia, the wettest and least sparsely populated part of the country, where demands for land reform are strongest. People there want jobs or, failing that, secure tenure on small plots of arable land near home. The government could provide this by redistributing some 8m hectares of state-owned land.

"Land reform in these communal areas is the key issue for poor farmers," says Dirk Hansohm, an economist in Windhoek. Donors would happily finance resettlement on such lands. But Mr Nujoma is not particularly interested. Why? Perhaps because none of those arrogant white farmers has a plot in the north. ■

Oil in Chad

Useful stuff, maybe, for once

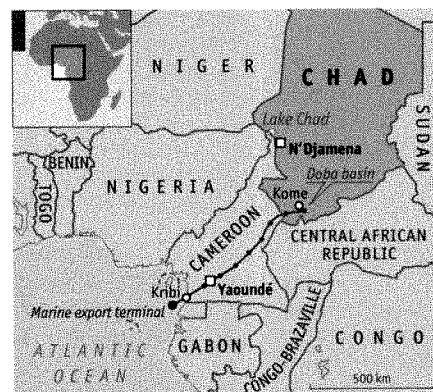
KOME

A novel scheme to extract oil without fuelling corruption or bloodshed

ALMOST every African nation blessed with copious minerals is also cursed with some form of civil unrest. Rebels, regular armies, and sometimes foreign armies too, slug it out for control of oil or diamonds. Nor does natural wealth promote good governance. A regime with oil is less accountable to ordinary citizens; it does not have to collect their trifling taxes or meet their tedious demands. A portion of the petrodollars must be spent on the army to keep the masses in line, but the rest can be split among the political elite.

But not, it is now hoped, in Chad, where the World Bank has devised a new scheme to ensure that oil profits are spent wisely. The stakes are high: a consortium led by ExxonMobil has just started pumping oil in the country's Doba basin, and the government's oil revenues are expected to reach \$80m-\$140m after 2003. What is novel about the plan is that the consortium will not pay the money directly to the Chadian government. Instead it will go into an offshore account. To get it, the government will require consent from an independent committee, which has to co-sign all cheques, and will do so only if the government spends the money on health, education or basic infrastructure.

The World Bank sees the scheme as a model for how oil firms can function in unstable parts of Africa. Many are eager to diversify out of the Middle East, and so



have an eye on Africa's vast untapped reserves. In the past, firms have tended to make under-the-table deals with corrupt African leaders and then claim that, as private companies, they cannot be held responsible for how the governments they bankroll spend the cash. It is not an absurd argument—no oil firm has the power to bring peace to Sudan or to clean up Nigerian politics. But under pressure from activists, some companies are trying to exert a bit of influence. BP, for example, tried last year to promote transparency in Angola by revealing how much it paid to the thoroughly corrupt government there.

In Chad, ExxonMobil agreed to work with the World Bank, and to submit to its stern demands for transparency and ►►

► accountability. It thus hopes to placate environmental and human-rights lobbyists, who have been loudly critical of the project. ExxonMobil says that its pipeline, which stretches 1,000km (600 miles) through virgin rainforests to the coast of Cameroon, is the largest-ever private infrastructure investment in sub-Saharan Africa, costing \$3.7 billion. The oil company, which faces plenty of risks on the ground in Chad, does not want the pipeline to become a global public-relations disaster.

Even before they had oil to fight over, Chadians had been at war with one another almost constantly since independence from France in 1960. Hissène Habré, a president of Chad in the 1980s, tortured and killed tens of thousands of his own people, stopping only when overthrown, in 1990, by General Idriss Déby. Mr Déby is still in charge, having rigged a presidential election last year. His government and army are dominated by Muslim northerners, mostly from his own tribe.

Better than fighting each other

Various groups continue to rebel against the regime, but fighting in the Christian and animist south, where the oil is, has eased since 2000, when the army killed the main southern rebel leader. Southerners are still fractious, but now direct their complaints mostly at the oil firms. The arrival of hordes of well-paid expatriates has caused prices of basic goods to soar to levels many locals cannot afford. The oil firms do provide jobs, but only about 3,000 of the 10,000 workers on the project are Chadians, and most will be laid off when the pipeline is completed next year. In the meantime, schools are finding it harder to function because teachers are taking better-paid jobs with the oil company. There are frequent strikes as well as reports of sabotage.

ExxonMobil is spending \$8m to compensate those living along the pipeline and has agreed to a slew of social and environmental conditions set by the World Bank and others. Environmentalists still complain that the pipeline will damage the Cameroonian rainforest, and other worries remain. The pipeline will be able to withstand a fair amount of unrest, not least because it is being laid underground.

But many doubt the government's good intentions. Its first taste of oil money, in 2000, was spent largely on arms. Mr Déby's excuse was that he was facing a fresh rebellion in the north. Were a rebellion to occur in the future, a little-discussed clause in the revenue-sharing agreement would allow him, once again, to splash out on weaponry. Even so, the World Bank insists that Chad, unlike its neighbours, will put the bulk of its oil windfall to better use. "Chad has to be different," says one World Bank official, "because we're staking our reputation on it." ■

Angola

Rebels in search of house and job

SAMBO

The war is over, but what can be done with all the ex-rebel soldiers?

HOME improvements are all the rage in Sambo, a "quartering area" for former UNITA rebels in central Angola. Ex-guerrillas are mud-plastering their huts, using strips of bark to weave patterns into the walls. It beats living in the bush, where most have spent the past two decades. And some, after years of looting, have turned to honest trade. A makeshift shop sells home-made flour sieves, a few pairs of corduroy trousers, and a single pink bottle of hand lotion.

The camp at Sambo is one of many. Since April, when the government made peace with an all-but-defeated UNITA, 35 have been set up, to ease the rebels' reintegration into Angolan society. About 5,000 UNITA soldiers and officers are to be given posts in the Angolan army. The remaining 80,000 are now officially civilians but, in practice, they still take orders from UNITA functionaries, and have an unknown quantity of weapons stashed away.

They are supposed to have surrendered their guns to the government, but officials will not say how many have been received. The tallies from individual quartering areas give some clue: for every four soldiers, an average of less than one weapon has been handed in. Officers claim this is because so many were "lost in the bush". This excuse is less lame than it sounds. UNITA was in disarray by the time its leader, Jonas Savimbi, was killed in February, thereby precipitating peace.

For now, Angola is enjoying a post-war honeymoon. Ancient lorries and donors' jeeps shuttle between the country's shattered towns, dodging potholes but no lon-

ger fretting that they might be ambushed. How long will peace last? Only as long, some drivers fear, as the demobilised rebels believe that the government will give them what it has promised: vocational training, and help back into civilian life.

The regime has enough money to keep its promises, but lacks the necessary know-how and political will. It plans to close the quartering camps next month, and send the former guerrillas back to their long-abandoned home villages. Aid workers fear that this could leave many of them destitute, hungry and restless.

The United Nations is trying to help. It serves as a giant soup kitchen for 4m displaced people, and also, recently, for the 300,000 residents (rebels and their families) in the quartering areas. The government would probably prefer that it limited itself to such uncontroversial charitable activities. But the UN still has other tasks.

On August 23rd, the government and UNITA agreed to implement, under the UN's watchful eye and within 45 days, the terms of an earlier peace deal, under which UNITA was to stop fighting in return for a clutch of cabinet posts and ambassadorships. UNITA wants to keep the UN involved for as long as possible, to prevent the government from pushing it around. The rebel group claims to be penniless, having lost control, it says, of the diamond fields that used to finance its guerrilla war. Some of its leaders are doing well, though: at least one UNITA general has formed a joint mining venture with an old adversary from the army.

After the 45 days are up, UN staff are uncertain how much influence they will continue to wield. Elections are scheduled for 2004, but as things stand, Angola remains, in effect, a one-party state. Opposition parties are splintered and harassed. Most of the media are state-controlled. Ruling-party flags fly over the camps where the UN distributes food, with the sole exception of the UNITA quartering areas. And these are soon to be closed. ■



Home-making, but strictly temporary



Germany's foreign policy

Why Gerhard Schröder has gone out on a limb

BERLIN

For the first time since the second world war, Germany's foreign policy is distinctly at odds with America's

UNTIL recently, Germany was one of the United States's best friends. The Americans could rely on its enthusiastic moral, if not military, support in most global matters. Within hours of the terrorist attacks on the United States a year ago, Gerhard Schröder, Germany's chancellor, was among the first to pledge his "unlimited solidarity", describing the event as "a declaration of war against the entire civilised world". But now he has categorically rejected any German support for an American-led attack on Iraq, even if backed by a United Nations mandate. The relationship that has been the cornerstone of German foreign policy since the second world war is under severe strain. Though several European governments feel much the same towards Mr Bush's policy, Germany's has gone furthest out on a limb.

What has happened? Over his four years as chancellor, Mr Schröder has presided over democratic Germany's coming of age in foreign affairs. He courageously led his country into its first armed conflict (in Kosovo) since the second world war, then into its first war outside Europe (in Afghanistan), on both occasions risking his government's downfall. "The days when Germany could stand timidly on the sidelines, declining to participate in foreign military missions, are irrevocably over," the chancellor declared after last September 11th.

Until now, Mr Schröder has always

been very firm that Germany would never act on its own. But suddenly he is talking of a new "German way" in foreign policy, with echoes—alarming to some—of Germany's *Sonderweg* (special way) in the 1930s. This worries quite a few of Germany's friends. It is not just what Mr Schröder has said about the United States and Iraq, but also the way he has expressed it. Germany, he declared, rejected any American military "adventures" in Iraq. While willing to help press Saddam Hussein into letting UN weapons inspectors back into Iraq, Germany was not prepared "to play around" with war.

Edmund Stoiber, the conservative challenger for chancellor, has been more nuanced, accusing his rival of sacrificing Germany's ties with its most important partner for electoral gain. Mr Schröder's Social Democrats are running neck-and-neck against the Christian Democrats in the run-up to the general election on September 22nd. Every vote counts. Whereas a large majority of Germans backed the war against al-Qaeda in Afghanistan after September 11th, most, especially those on the left, are dead against one with Iraq. At campaign rallies, Mr Schröder and Joschka Fischer, his Green foreign minister, always get the loudest cheer for their stand on this issue of "war and peace".

Germans are not anti-American. They admire many facets of American life, share most basic values, and generally regard the

United States as their key ally. But Mr Bush's administration is not getting a good German press. The list of gripes is long: many Germans deplore Mr Bush's hostility to the International Criminal Court; his attitude to the environment; the death penalty; unfettered American support for Israel against the Palestinians; genetically modified foods; farm subsidies; the Americans' apparently growing unilateralism; and now its policy on Iraq. At home it does Mr Schröder no harm to be bravely standing up to the perceived American bully.

It would be wrong to dismiss his stance as pure vote-catching. He and many other Germans think an attack on Saddam Hussein would be an error. Earlier this month Mr Schröder told the *New York Times* that he was not convinced that Mr Hussein posed an immediate threat. A strike against Iraq, the chancellor argued, would unsettle all of the Middle East, destroy the international coalition against terror built up after September 11th, and perhaps even push the Iraqi dictator into the very rapprochement with Islamic extremists that the United States fears. Moreover, he says there has been no American effort to analyse the consequences of such an attack nor to plan any clear strategy thereafter.

He singled out what he claimed was America's "change of strategy" at the end of August, when the vice-president, Dick Cheney, said that the Americans' aim was to overthrow Mr Hussein, not just to get the UN's weapons inspectors back in. "How can you exert pressure on someone by telling them that, even if you accept our demands, we will destroy you?" he asked. He was miffed, too, by lack of consultation. "It just isn't good enough to learn from the American press about a speech which clearly states: 'We are going to do it, no matter what the world or our allies think.' That is no way to treat others," he said. ►►

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Above all, Mr Schröder rejects America's claimed right to pre-emptive action against Iraq. On this score he is not alone among Europeans. France's president, Jacques Chirac, has called Mr Bush's doctrine "extremely dangerous". German diplomats echo Mr Chirac's argument that other countries might demand a similar right to pre-emptive action: India against Pakistan, for example, or China against Taiwan. "A few principles and a little order are needed to run the affairs of the world," Mr Chirac explained, to German nods of approval. But, unlike Germany, France has not ruled out the possibility that it might take part in an attack against Iraq, provided the UN approves.

Germany is the only member of NATO or the EU to have done so. Asked in a televised debate with Mr Stoiber last weekend whether he might change his mind about Iraq after Germany's election, Mr Schröder said categorically that he would not.

With his brash megaphone diplomacy, Mr Schröder seems to have painted himself into a corner from which it will be hard to unstick himself without looking silly. If the Americans do hit Iraq without German support but with Britain, France and others alongside, Germany could find itself summarily dismissed from its new hard-won place at the top table of nations.

Mr Stoiber, meanwhile, is still hedging his bets. He says he won't rule out "any options", but at the same time says he does not want "any military measures and certainly not with German participation". He, too, is mindful of votes. But once war begins, he is a lot more likely to fall into line behind the Americans. If Mr Schröder remains chancellor, he may have a hard time rebuilding the transatlantic bridge. ■

Austria's collapsing government

Back to square one

After the collapse of Austria's right-wing coalition, what next?

THE fall this week of Austria's first purely right-wing government for three decades may well mark the end of the political road for Wolfgang Schüssel, the country's chancellor for the past two-and-a-half years and leader of the mainstream conservative People's Party. It is unlikely, however, to curb the ambition of Jörg Haider of the populist Freedom Party, the outgoing coalition's second strand, to win the country's top job some time in the future. Meanwhile the Social Democrats, who have run Austria for most of the past century, usually as the main partner in various coalitions, seem likely to come back



Can Haider be restrained forever?

into power by the turn of the year.

What has Mr Schüssel, who was vilified by the left at home and abroad for ditching the Social Democrats and bringing the Freedomites into his coalition, achieved? For one thing, he had hoped to cut his right-wing rivals down to size, by forcing them to drop their xenophobic populism once they were locked into power. He had also hoped to tame their rabble-rousing leader, Mr Haider, who was formally made to opt out of national politics and retreat to the governorship of the southern province of Carinthia, a job he already had as his party's national boss. That was the price the Freedom Party had to pay for joining Austria's government.

Mr Schüssel probably succeeded in his first aim. The Freedom Party has slumped in the polls from the 27% that it won in the last general election, in late 1999. But he has plainly failed to emasculate Mr Haider. The 52-year-old maverick continued to call many of the shots within his party from his southern Alpine redoubt. It was when his party colleagues, such as Susanne Riess-Passer, who had become the country's vice-chancellor and the party's formal leader, and young Karl-Heinz Grasser, who became finance minister, refused to do Mr Haider's bidding that rows broke out in their party. These eventually, this week, led to the coalition's collapse.

Until then, the centre-right-cum-hard-right coalition had chalked up a number of gains. Last year it just about managed to balance the budget. It negotiated compensation for victims of the Nazi period during Austria's union within the German Reich under Hitler. It also enacted some necessarily painful reforms that the previous Social Democratic-led coalition had fumbled. For instance, it raised the retirement age, changed the system of sever-

ance pay that had impeded job mobility, and made university students pay for part of their tuition. And it further weakened the old patronage system of *Proporz*, whereby many public-sector jobs, from drivers and janitors to head teachers and diplomats, were carved up between members of the two main parties.

Still, the Freedom Party also prevented Mr Schüssel's lot from enacting various other reforms, such as the liberalisation of shop-opening hours. And it forced the government to increase Austria's already generous allowance for parental leave. In most respects, however, the government did not seem particularly in hock to the populists. The outrage expressed by many other European Union governments when the coalition took power has for the most part looked misplaced.

But it was precisely the new-found respectability of the Freedom Party's people in government that began to niggle Mr Haider, especially as his party's popularity, based largely on protest in opposition, started to slide. While Mrs Riess-Passer stopped listening to him, sounding sensible and moderate on a visit this year to the United States, he resorted to his rebellious old ways by flying off twice to see Saddam Hussein in Iraq and having cosy meetings with Belgium's ultra-nationalist nasties. He accused Mrs Riess-Passer of being "duped" by her coalition partner and then engineered a party coup that forced her and three of her closest Freedom Party colleagues in the government to resign. Mr Schüssel ended the rumpus by calling a general election that will probably be held in November or early December.

Being the junior partner in a moderate government had weakened the appeal of Mr Haider's party to its core constituency, disgruntled blue-collar workers and oth-

ers, such as small farmers and shopkeepers, who feel threatened by modernisation. Hence Mr Haider's decision to adopt his old posture as opposition leader. He had balked at the coalition government's decision to put off tax cuts to pay for recent flood damage. Most notably, he has noisily recanted his party's enforced and grudging support for the expansion of the EU to take in countries to the east.

But Mr Haider is unlikely to win back all the support his party lost by joining the government. In any case, he must first regain his grip over the party at what is likely to be a rowdy gathering later this month. After re-establishing himself as the opposition's main leader, he probably hopes to have another serious shot at the chancel-

lorship in, say, 2006.

The latest opinion polls put the Social Democrats well ahead in today's field, with around 35% of likely votes. Mr Schüssel's People's Party stand at around 29%, Mr Haider's Freedomites at less than 20% and the Greens at about 12-14%. If the two big parties do, as usual, come out on top, Mr Schüssel is unlikely to stay on as chancellor. The Social Democrats' Alfred Gusenbauer is tipped to lead a new coalition, either with the People's Party or the Greens. Though only 57, Mr Schüssel would probably bow out as his party's leader. But Mr Haider will probably stay on his perch, preaching populism, occasionally pandering to xenophobic prejudice, and waiting for another chance. ■

Meanwhile, thousands are smuggled in from Africa, the Middle East and Asia to swell the ranks of the *sans-papiers*—those who have no identity papers to give them a right to residence.

Once arrived, illegal immigrants are unlikely to leave. That holds true even of the minority who are arrested. In 2000, for example, some 43,739 foreigners were given their marching orders, but only 9,230 were expelled. In 1996, when the right was cracking down, some 28,000 foreigners with the wrong papers or no papers were arrested in Paris—but 22,000 were quickly released and only 1,700 left the country.

So what will Mr Sarkozy's balanced policy amount to? Though there will surely be no blanket legalisation of the kind advocated by Jack Lang, a former Socialist minister, to end "inhumane and absurd situations", a great many of the *sans-papiers* will probably get their papers, and perhaps sooner rather than later. One reason is that Mr Sarkozy, saying the authorities previously acted with "excessive administrative zeal", is setting a new tone. The police chief of Paris, for example, now promises to look "case by case" at demands for legal status, and to do so with "pragmatism and humanity".

The second reason is that the rules have already proved flexible enough to allow for such pragmatism and humanity: of the 140,000 foreigners who sought to "regularise" their status when the left came to power in 1997, some 80,000 succeeded. Marriage to a French citizen; children born in France; severe ill-health; "personal or family links in France"; or simply residence, albeit illegal, in France for ten years or more: all these can give a *sans-papier* the right to reside. As long as the civil servant making the decision did not vote for the immigrants' foe, Jean-Marie Le Pen. ■

France's illegal immigrants

A new balance

PARIS

France's new government is trying to create a "balanced" immigration policy

HOW many illegal immigrants reside in France? Whatever the true figure—200,000 to 400,000, according to various estimates—they have been enough to discomfort a string of governments by demanding the right to stay. In 1991, for example, a group of unsuccessful Kurdish asylum-seekers embarrassed the Socialists with hunger strikes; in 1996 the centre-right government of Alain Juppé sent in riot police to dislodge 300 Africans, mostly from Mali, who had sought refuge in a Paris church. And now comes the turn of the centre-right government of Jean-Pierre Raffarin: thousands of illegals have greeted its return from holiday with a series of street demonstrations in Paris and other cities—and another is promised for September 28th.

All of which could mean a nasty political headache not just for Mr Raffarin but more particularly for his interior minister, Nicolas Sarkozy: a hard line would alarm those many French citizens who take human rights seriously; a soft line would give ammunition to an extreme right whose presidential candidate, Jean-Marie Le Pen, last April got more votes than Lionel Jospin, the Socialists' then prime minister.

Hence, last week, Mr Sarkozy's careful choice of words: "France needs immigrants, but France cannot and should not welcome all immigrants." As the minister went on to argue, immigration is an issue all too often taken "hostage" both by the "fanatics of zero immigration, which is a nonsense given that France is built on its diversity" and by liberal "extremists" whose call for automatic legalisation

would only breed xenophobia. In other words, France must have "a balanced policy, without pretence or hypocrisy".

No hypocrisy? For sure, France does need immigrants. Southern wine-makers and fruit-growers, for instance, complain that they cannot get enough workers, despite jobless rates of over 9% of the workforce, while United Nations statisticians say that France would need 1.7m immigrants a year to maintain its demographic status quo. In accordance with European Union policy, however, the country does its best to keep out non-EU migrants.



My papers, please

Sweden's coming election

Unusually tight

MALMO

Sweden's leader is having to fight harder than expected to keep his job

A MONTH or two ago Goran Persson was on cruise control. Buoyed by a purring economy and personally popular, Sweden's Social Democratic prime minister looked comfortably set to win a general election on September 15th. Yet in a few weeks, his aura of invincibility has waned. Pollsters say that a four-party alliance led by the Moderate Party, as Sweden's conservatives are known, could yet get as many votes as the likely combined tally of Social Democrats, Greens and the Left, as the ex-communists are called. But the odds still favour Mr Persson to stay in power at the head of his minority government, which includes the Greens and relies on a pact for votes in parliament with the Left.

Mr Persson's stolid election campaign has smacked of complacency, while the Moderates, together with the free-market Liberals, the Christian Democrats and the rural-minded Centre Party, have waged an energetic crusade calling for sweeping tax cuts and better-run welfare services. That the quartet can even dream of an election victory owes much to the revitalised Liberals. Six months ago they looked hard pressed to get the minimum 4% of the national vote to win any seats in parliament, but the latest opinion polls give them around 13%, making them the third party after the Social Democrats, on around 36%, and the Moderates, on 20% or so.

The Liberals' renaissance began when their leader, Lars Leijonborg, said that immigrants should have to pass a Swedish language test before getting citizenship. Integrating immigrants is an increasingly vexed issue. Unemployment among newcomers is high and the growth of ghettos outside the country's main cities worries many indigenous Swedes. While the main parties have largely steered clear of the issue, Mr Leijonborg touched a raw nerve.

Unfortunately for the combined conservative opposition, the Liberals' gains are partly at the expense of their allies, in particular the Moderates, who are predicted to fall short of the 23% share of the vote they won in the last election, in 1998. The non-socialist block probably needs an outright majority of seats to oust Mr Persson. That still looks beyond its reach.

Moreover, many Swedes are sceptical about the alliance's plan for tax cuts, in particular the mammoth package suggested by Bo Lundgren, the Moderates' leader, who promises to reduce taxes by SKr130 billion (\$14 billion) over four years,

A Spanish wedding

End of an era?

MADRID

Was the grandeur of the wedding of the prime minister's daughter a mistake?

TELLING error of judgement by a politician losing touch with reality, or a proud father doing his best for his beloved only daughter? Spaniards differ over the slap-up wedding hosted last week by their prime minister, Jose Maria Aznar, but the event certainly set tongues wagging. More than 1,000 guests gathered at Philip II's majestic El Escorial monastery for a nuptial mass conducted by Spain's cardinal-primate.

"A wedding fit for a princess?", mused a Barcelona paper. Well no, not quite. But it certainly wasn't a private family affair either. Spain's king and queen were there, along with the British, Italian and Portuguese prime ministers. So too were a galaxy of jet-setters who grace the pages of Spain's so-called "press of the heart" but would rarely be invited to attend a truly state occasion. The entire government was there too, but no one from the opposition.

It was all rather out of character for a man whose own austerity is legendary. Mr Aznar paid around €200 (\$195) a head for a post-nuptial dinner and dance at a country estate that was loaned free of charge, and for a joint stag-and-hen party a couple of days earlier at a fashionable Madrid discotheque for 800 people. The Spanish taxpayer picked up a tab for security that cost, it is said, €120,000.

Look to the wife, say some. Look to the new son-in-law, insist others. Alejandro Agag is a longstanding prime-ministerial aide turned banker, a decade older

than his 20-year-old bride. Smooth and ambitious, he cultivated the rich and powerful while working on Mr Aznar's behalf in Brussels. Some of the more notable guests, such as Rupert Murdoch, a media mogul, and Silvio Berlusconi, a tycoon who now runs Italy, are Mr Agag's own pals.

In any event, some people in Mr Aznar's People's Party are twitchy. Ordinary Spaniards may think their prime minister had gone over the top. Not so, says Mr Aznar. Apparently determined to leave office in 18 months' time, he has brushed off the charge that the wedding was an end-of-era misjudgment. All the same, says a critic within the ruling party, "the Aznars wouldn't have dared organise an event like that when we were first elected."



Daddy has a lot of friends

if elected. He says he would save SKr80 billion by cuts in the public sector, though he has yet to identify where exactly he would wield the axe. He would save the other SKr50 billion, he says, by generating higher growth through lower taxes.

Mr Lundgren says Sweden's taxes, which are the highest of all countries in the OECD, foster an anti-enterprise culture. He points to several big Swedish companies that have moved their headquarters abroad as evidence that high taxes are harming business and stifling job creation.

But many Swedes, not just on the left, fear that big tax cuts would hit welfare. This week his supposed allies—the Liberals, the Christian Democrats and the Centre Party—all implied that Mr Lundgren's plans were too radical. Mr Leijonborg bluntly labelled them "unrealistic".

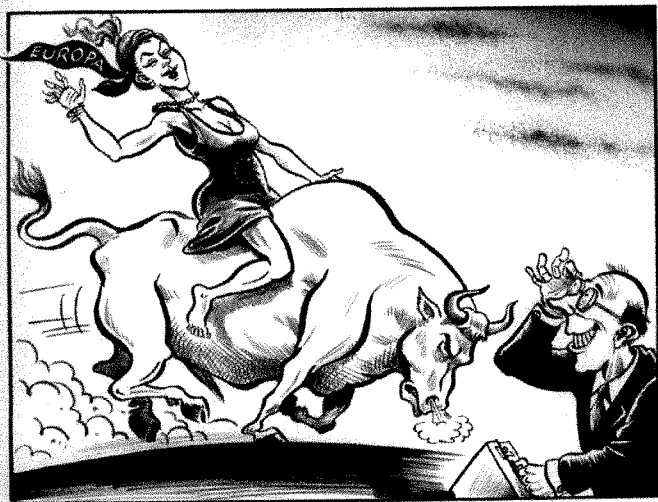
In any event, Mr Persson, who took office in 1996, can cite a fair record. Since

1999, Sweden's economy has grown by nearly 4% a year. This year it may swell by only 1.9%, but that is above the EU average. Inflation is running at 2.2%, unemployment has dipped to 4.3%, interest rates are low. Consumer spending is perky, despite a bearish stock market and big problems at Ericsson, the telecoms company that is Sweden's biggest private-sector employer.

Mr Persson has deftly handled his minority government in parliament. Most Swedes consider him reliable and decent. Still, if the election result is tight but he still comes out on top, he may find the Greens and the Left unusually tricky. They are both hostile to European integration and argue against joining the euro, which Mr Persson wants Sweden eventually to embrace. Now both groups say they must have posts in the cabinet. Mr Persson is against that too. Even if he wins, he will face an awkward autumn. ■

Charlemagne Why Brussels isn't boring

After all, an entirely new system of running a continent may be afoot



ANNOUNCE that you work as a journalist in Brussels and you are likely to get a pitying look and a polite inquiry. "Do you find that interesting?" The implication is that only fans of watching paint dry could possibly answer "yes". Right now the contrast between the dramas elsewhere in the world and the humdrum day-to-day business of Brussels is particularly stark.

As the world commemorated September 11th and President George Bush prepared to address the United Nations, the European Commission went about its normal tasks. It announced that it is looking at ways of harmonising car taxation; it trumpeted the fact that 80,000 pages of European Union law are about to be translated into nine new languages; and it signed a memorandum of understanding on "intermodal Pan-European corridor VIII"—ie, some roads and railways linking Albania, Bulgaria and Italy. Even the EU's occasional scandals tend to have a peculiarly dull stamp. The Americans had Monica Lewinsky. By contrast, the biggest scandal to hit Brussels this year is an accusation by the European Commission's chief accountant that the organisation has failed to use double-entry book-keeping.

But while the day-to-day details of EU affairs can be grim, the big picture is fascinating. Really. The Union has recently embarked on projects so ambitious that they challenge fundamental assumptions about both politics and economics. The euro is the first-ever attempt to create a real international currency (though Charlemagne himself had similar ideas). Until the new coinage began to jingle in pockets in 12 EU countries in January, it had always been the case, bar a few trivial exceptions, that a currency was issued by a country and backed by a national government and a central bank. With the euro, all that has changed. Will it lead to an economic government in Europe with a much bigger budget and tax-raising powers or will it establish a new way of managing currencies and monetary policy? This is not just a debate to engross economists. It will have weighty consequences for 300m-plus people who now use the new currency—and may inspire similar experiments elsewhere.

Not content with reinventing monetary economics, the EU is also remodelling the basic building block of global politics, the nation-state. It was Europe that invented the model in the first place, and Europe that now seems to be disinventing it. By joining the EU, European countries accept the supremacy of Euro-

pean law over national statutes. The EU tells the French when they may shoot small birds, the British how many hours they can work in a week, the Germans when they can subsidise their businesses. Delegates to a European convention are now pondering demands for a federal constitution for the EU.

Some believe that the Union is in effect turning into a new country—a United States of Europe—that will one day exercise power much as a traditional nation-state does. Others argue that the EU is doing something both less dramatic and more innovative. It is busy acquiring many of the characteristics of a nation-state, while actually creating something newer and more complicated. Either way, the consequences for the rest of the world will be drastic. A United States of Europe, if it ever came about, would profoundly shift the global balance of power. But a new hybrid political form, dependent on international law and deep co-operation between the older states, would create a political model which would challenge traditional assumptions about government all over the world.

So if the EU is so interesting, why does it seem so dull? Partly because most of the Union's formal day-to-day powers are technocratic: a merger to be approved or turned down; a trade dispute to be resolved; an environmental directive to be issued. But there is more of a connection between the drab details and the big picture than is often realised. Eurosceptics often argue that the integrationists promote their ambitions by stealth—by dressing up big political changes as mere technical adjustments. This argument can mislead. Sometimes it even smacks of paranoia. Sometimes, however, it is true. In a frank moment, Jean-Claude Juncker, Luxembourg's prime minister, once described the EU's "system". "We decide on something, leave it lying around and wait and see what happens," he explained. "If no one kicks up a fuss, because most people don't understand what has been decided, we continue step by step until there is no turning back."

Brilliant, but also slightly sinister

What Mr Juncker and those who think like him are trying to do is, in essence, to drown opposition to European federation in a mass of technical detail, to bore people into submission. As a strategy, it has gone a long way. The greatest single transfer of sovereignty from Europe's nations to the European Union took place, in 1985, as part of the project to create a single European market. Even Margaret Thatcher, not usually slow to spot a trick, later claimed that she had not fully appreciated the ramifications of what she was then signing up to.

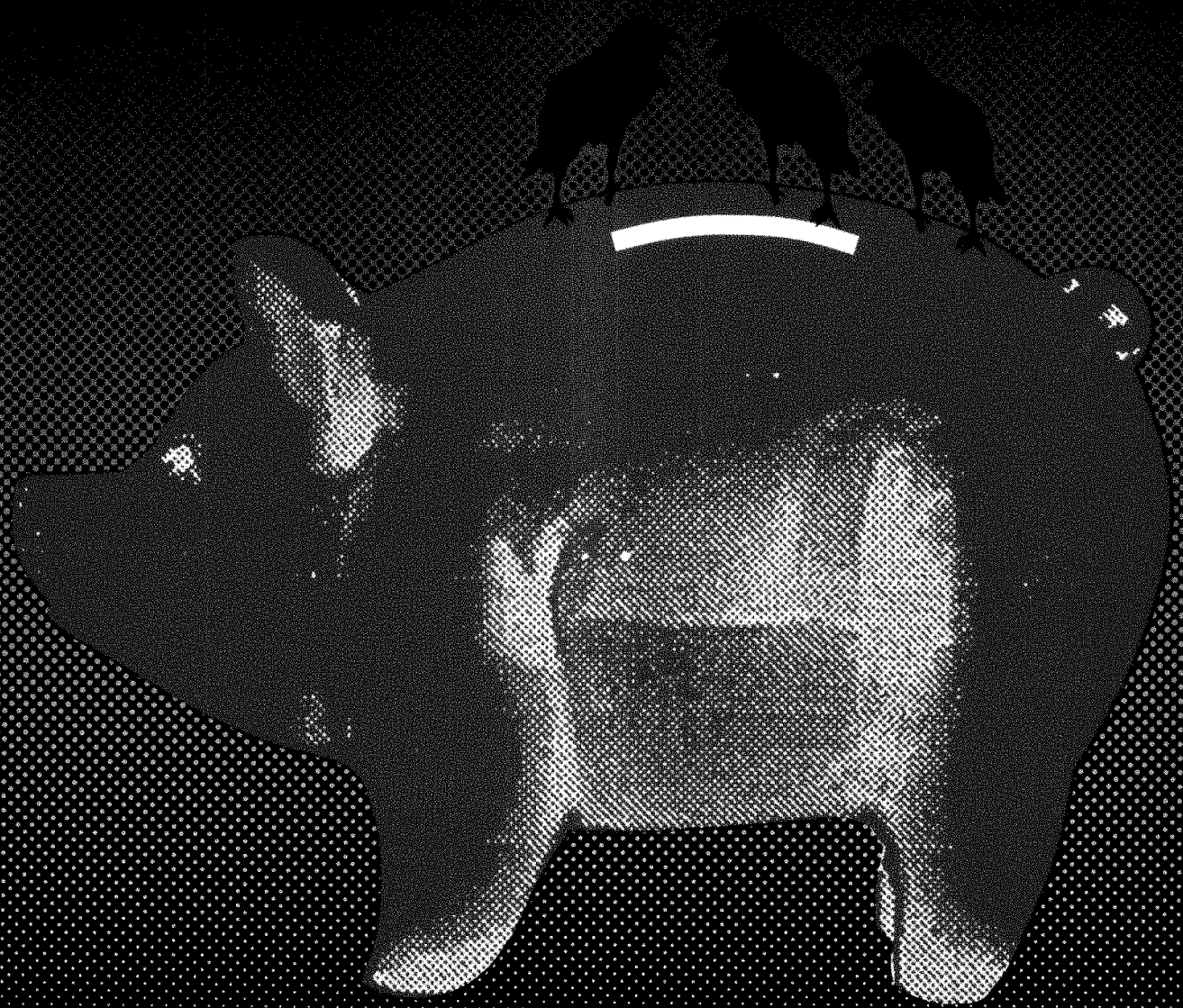
But there are signs that this strategy of integration by stealth has run its course. EU politicians and civil servants are genuinely rattled by mounting evidence that their Union is seen as remote and overbearing. They hope that their new convention will help them to "reconnect" with ordinary Europeans. In the process, that will raise basic questions about national and personal identity. Do people yet "feel European"? Or are national identities still much stronger? How far can the EU stray into sensitive new areas like defence and internal security?

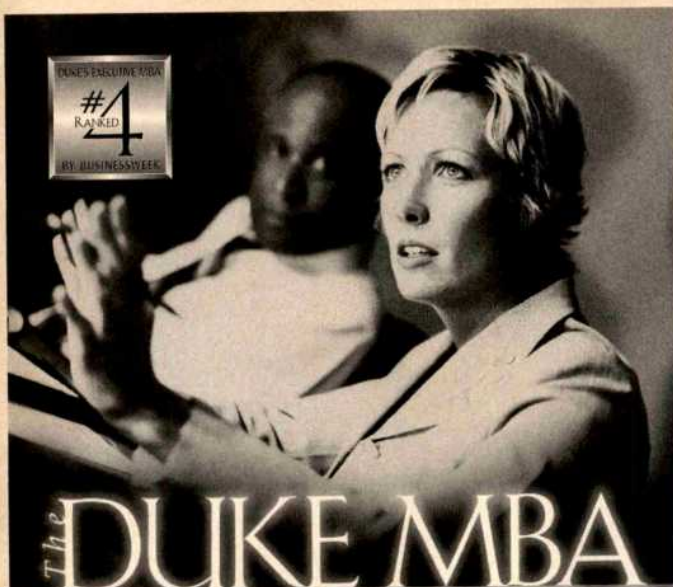
In dealing with such issues, the conventioners will also have to start addressing the question of whether the EU is a state in the making or some new form of political organisation. And then there is another possibility, little discussed in Brussels. The whole enterprise may ultimately prove impossibly complicated and begin to creak and break apart as a result of its internal contradictions. Now that really would be interesting. ■

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After the chaos

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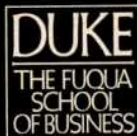
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After the chaos

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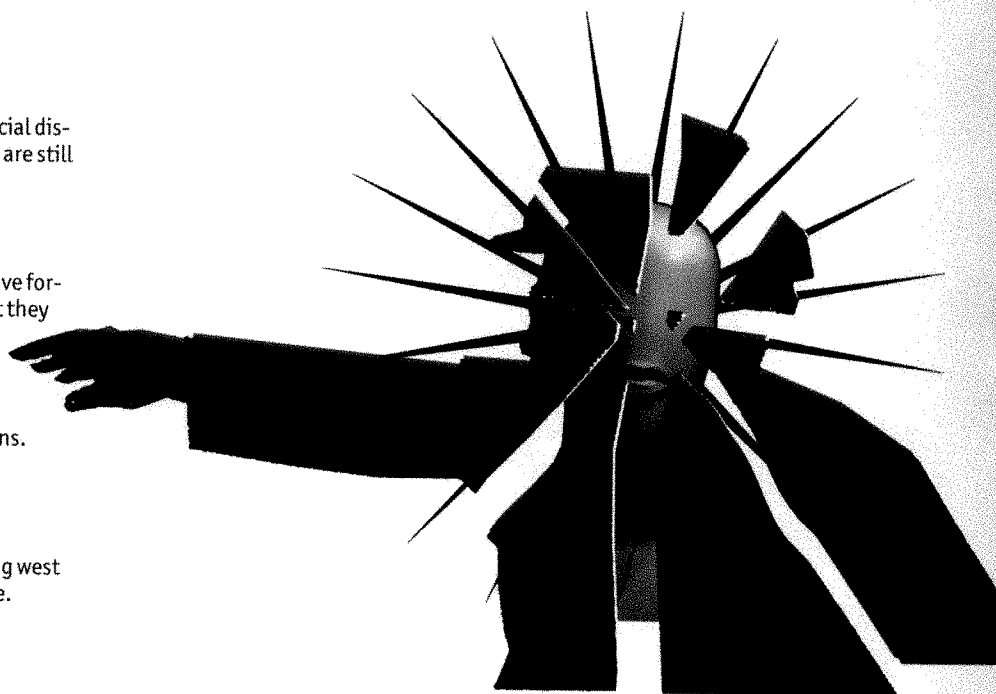
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Suddenly everyone wants to harness the power of consumers. But they are still thin on the ground. Page 15



To prepare for accession to the European Union, Central European countries need to speed up reform of their financial sectors. But old habits die hard, writes David Shirreff

"NEVER ask a man where he made his first million," advises a stockbroker in Prague. Ten years of chaos in Central Europe (here defined as the Czech Republic, Hungary, Poland, Slovakia and Slovenia) and points east, as a dozen countries ripped up communism in favour of market economics, allowed many opportunists to get rich quick. Some did so honestly; many more cheated, bribed and stole from the state or small investors, using conniving banks as a source of everlasting loans and a place to wash their money.

That era is coming to an end, at least in the more advanced countries. Emerging from the chaos are new structures that are beginning to resemble the financial systems in Western Europe, complete with banks (mostly foreign-owned), stockmarkets, mortgages and pension funds, bank supervisors, securities commissions, property laws and governance codes.

In this brave new world, why question too closely how some people, many of them now ministers, top managers and pillars of society, made their early fortune? It makes sense only if they are still up to their old tricks. When corruption persists at the top, it percolates throughout the economy; people do not trust their leaders; they hide their money; they expect to pay

and receive bribes; and banks do not trust their customers. To some extent that culture lingers on, even in Poland, Hungary and the Czech Republic, soon to become members of the European Union.

But nowadays the prospect of EU accession is prompting even corrupt leaders to pay more attention to reform. Ten countries selected for the first wave are racing to complete the requirements laid out in 31 "chapters", which include institutional reform, new laws, new tax regimes and anti-corruption measures. Hopes of accession, and fears of being bumped off the list, are concentrating minds.

Some former ministers and company bosses who lined their pockets in Poland and Serbia are now in jail. Many more of those formerly on the take are walking free. But for now everyone is inclined to draw a line and concentrate instead on moving towards better, cleaner, fairer and more efficient financial systems. The rewards include cheaper capital to fuel the economy and more saving by trusting consumers. Some reformers, such as Leszek Balcerowicz, the governor of Poland's central bank, think that financial reform can improve even such things as health care and income distribution.

At the heart of these reforms are the ►►

Acknowledgments and sources

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The following sources proved particularly useful: "Financial Transition in Europe and Central Asia", World Bank, 2001, especially chapter 3 by Lajos Bokros; "The Financial Integration of an Enlarged EU: Banking and Capital Markets", European Investment Bank, 2002; "Transition Report 1999", EBRD; "Transition report update", EBRD, May 2002; "Post-Communist Transition: Some Lessons", by Leszek Balcerowicz, Wincott lecture published by The Institute of Economic Affairs and Profile Books, 2002; Fitch Ratings' regular country reports on banking systems.



► banks. They account for about 80% of financial assets in these countries, in most of which securities markets are still widely underdeveloped. Communist bankers did not have to worry about credit risk because neither they nor their borrowers could go bust. After 1990, as market forces kicked in, almost every country in Central Europe had a banking crisis, but each dealt with its insolvent banks in different ways. The Czech Republic, for example, turned a blind eye for years, believing that banks were magical engines of growth. Not until the late 1990s did the Czech government privatise its big banks at huge expense—equivalent to 21% of one year's GDP.

Hungarian reformers were much quicker to cotton on that the banks needed new owners, new capital and new management. They began to privatise them in 1994, judging that the price was less important than getting them into responsible private (which meant mainly foreign) hands. Serbia started reforms only two

years ago, emerging from years of war and cronyism under President Slobodan Milosevic. Learning from the experience of others, it closed several of its biggest banks earlier this year, cutting off ailing industries from addictive soft loans. Such prompt action may save Serbia most of the huge expense—equivalent to between 10% and 25% of annual GDP—that delay has cost other Central European countries, but it put 9,000 banking staff out of work overnight. The dusty windows of disused bank branches stare down all over Belgrade.

Foreign umbrella

The other leg of banking-sector reform is foreign ownership. Only a handful of banks in Central Europe have shown that they can compete without the backing of a foreign bank, its risk-management systems, its range of products and its credibility. One of them is OTP, the biggest bank in Hungary. Once a savings bank with a monopoly of the retail market, it has thrived

because of good local management. Another, although not so well run, is Bank PKO BP in Poland, which also had a monopoly. Almost all other successful banks in the region are owned by foreign banks. Even Slovenia, which for years resisted big foreign investors for fear of being swamped by foreign capital, sold two big banks to foreigners last year, and is negotiating the part-sale of its biggest to a Belgian bank. Neighbouring Croatia has been the most outward-looking: 90% of its banking assets are foreign-owned.

In theory, this foreign ownership plugs the financial sector into the western world, bringing higher standards of governance and better access to capital. More competition means lower lending premiums, especially for small and medium-sized businesses. Foreign ownership also offers a fast track to new financial services such as mortgages and leasing. All of this increases the deployment of funds where they are needed, and coaxes savings from under mattresses and out of offshore accounts. The parent banks usually make a better job than local supervisors of overseeing their new subsidiaries. Often there is an implicit safety net: the parent will not let its offspring go bust, thus providing a lender of last resort for part of the financial system.

But banks cannot do it all. The big disappointment in Central Europe has been the slow development of alternatives: capital markets and private equity. Most of the countries built stock exchanges with great fanfare. Thanks to mass privatisations, some of them had thousands of companies listed. But new capital failed to arrive, or if money came in from abroad, it soon flowed out again as the fad for emerging markets lost favour. Worse, company shares, traded without enough disclosure and without enough volume to establish convincing prices, invited all kinds of market abuse and flouting of minority shareholders' rights. Only now are some of these problems being tackled in the few markets that are not dying a slow death.

On a larger scale, each local capital market is facing a choice: should it fight for its national identity, or append itself to a pan-European exchange? This is not just a question of patriotism. These countries are belatedly trying to build up funded pensions for their citizens. Arguably, a good chunk of those funds should benefit the local economy, rather than be invested in government bonds. Pension and insurance funds are vital to capital markets. They helped Chile build a robust market, and are beginning to do the same in Poland. ►►

It took time to recognise that countries emerging from communism desperately need small and medium-sized businesses. Some of them, especially former Yugoslavia (the rump of which, confusingly, is due to change its name to Serbia and Montenegro next year) had an artisan tradition, but in others private initiative was heavily discouraged. In Romania, to kill a pig for Christmas you needed permission from the mayor. The American government started the Polish-American Enterprise Fund in 1990 to foster small business, but the initiative spread only slowly to other countries.

The European Bank for Reconstruction and Development (EBRD) changed tack in 1994 and began lending to banks to en-

courage small businesses. This approach has been most successful in Russia, and in such unlikely places as Albania, Bosnia & Hercegovina, and Kosovo. The model is Germany's famous *Mittelstand*, the small and medium-sized companies that have proved such a trusty engine of economic growth there. But building up small companies takes time, enlightened loan officers and enforceable procedures for collecting loans and seizing collateral.

The countries of Central Europe do not have time. They are in a race to qualify for the greater Europe. Their legal systems and institutions are being wrenched into compliance with EU law, but their judges, lawyers and administrators find it hard to change their habits of 50 years.

All the same, after ten years of going up blind alleys, most countries in Central Europe appear to be moving forward. They can now choose from a menu of past experiments in banking and financial-sector reform, depending on what stage they have reached. But there are worries that they might go off the rails again. The banks are not lending enough, corruption is not dead, and bloodshed nearby is still a recent memory. Accession to the EU for all or some of the chosen ten still needs to be ratified at the EU's December summit in Copenhagen. Just imagine the financial shock to Poland, says one analyst, if its accession were knocked off course. Plenty went wrong in the past decade. Plenty more could go awry. ■

Grab and smash

IT SEEMS only yesterday that all of Central Europe was a giant construction site. In the haste to rebuild the economy, banks became the puppets of politicians and the new class of bosses; old factories were carved up by their former managers and machinery disappeared. Multilateral agencies such as the World Bank, the IMF and the EBRD tried their best to help at the birth of these new nations, but their money, too, often went astray.

Most countries made the mistake of attempting to do everything at once. The extreme case was former Czechoslovakia, with its "big bang" privatisation in 1992. Citizens were entitled to buy vouchers which they could exchange for shares in a bewildering choice of companies. Many put their trust in poorly regulated investment funds to make the choice for them. It was a wild era in which a few sharp individuals made fortunes, gathering enough shares to control companies. Many of the assets in which the funds invested also ended up in the control of the fund managers, some of them supposedly respectable western banks. This big-bang world did not bother with too many rules. Poland, Romania, Slovakia, Croatia and, famously, Russia chose voucher privatisations, with more or less similar results. The best that can be said is that these companies were taken off the state's balance sheet, and that investors lost an opportunity but not much money.

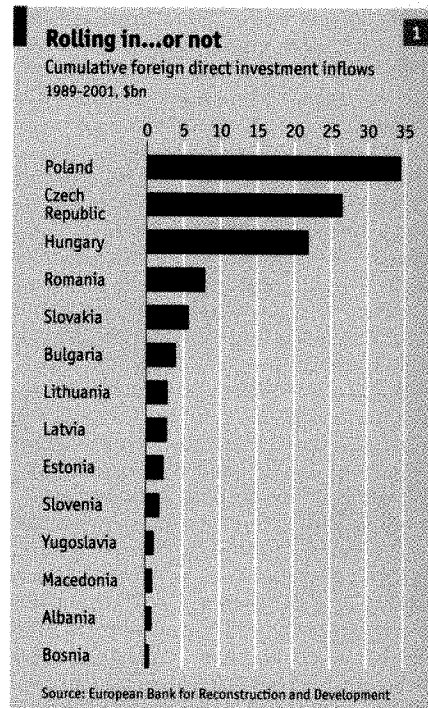
Hungary took a different road, preferring to sell companies to those with real money—that is, foreigners. Hungary's target was to attract \$10 billion of foreign direct investment in the first decade. It had already reached that level by 1995, even as other countries dithered over selling the family silver. Only towards the end of the decade did Poland and the Czech Republic catch up and attract more (see chart 1).

Voucher privatisations have since been condemned as a mistake, but the Czech Republic's second wave of privatisation was probably worse. It involved auctions, voucher privatisations or direct sales, often to the companies' own managers. The Czechs' aversion to foreign investment left their entire economy undercapitalised, with dire consequences for companies and their creditor banks.

Much the same happened in neighbouring Slovakia. Ivan Miklos, now deputy prime minister for the economy, recalls his experience on the supervisory board of Slovakia's National Property Fund, from which he resigned after a year: "In that year the fund sold 900 companies, but only one to a foreign buyer. It was impossible [for me] to get information about the sales." National property funds in several other countries were open to this kind of abuse, and even western companies saw opportunities that tempted them to throw corporate governance and rights of minority shareholders to the winds. Some

In the scramble for state assets, financial discipline was forgotten. Many countries are still paying for the resulting crises

of the canniest wheeler-dealers carried on for years, running companies and banks, bribing politicians and deceiving shareholders; they were suspected of being crooked, yet still feted by a public used to the ways of a communist elite. Some ended up in jail, or vanished. ►►



Perhaps surprisingly, the Czechs, the most disciplined and orthodox folk under communism, fell further from grace than others. Many now blame the extreme liberal ideas of their architect of reform, Václav Klaus, who was prime minister in 1992-98. He believed that freeing the market was more urgent than establishing an institutional framework. For a while western reform gurus, such as Jeffrey Sachs and Larry Summers, lent their support. But today most people believe that Mr Klaus's big bang created little economic growth, but a kleptocracy as bad as Russia's. Until last June the two main Czech parties had a so-called "opposition agreement" under which they refrained from digging into each other's recent history.

Except for some industrial dinosaurs, such as shipyards, metal plants and mines, most industry in Central Europe is now in private hands. That seems a useful outcome, even if ownership was not always properly transferred nor claimants' rights always respected. Noreen Doyle, vice-president of the EBRD, which has stepped around the dirty deals where it could, concludes: "You can't unscramble the past."

The sooner the better

The sick organ that used to keep these kleptocracies alive was the banking system. In Hungary in 1995, the finance minister, Lajos Bokros, and the central bank governor, György Suranyi, saw "deep corruption and cronyism in the banks", recalls Peter Mihalyi, who was then number two at the privatisation agency. Hungary is praised for having tackled its banks early, but it did so for largely pragmatic reasons. From 1992 to 1994 the government several times had to recapitalise the banks that it had spun out of the National Bank of Hungary. In the end it recognised the need for foreign capital. "The only reason we privatised the banks was because they were about to blow up," says Mr Mihalyi.

In July 1994 Bayerische Landesbank and the EBRD bought 25% and 17% respectively of the Foreign Trade Bank (MTB). Two years later the EBRD and GE Capital bought Budapest Bank, ABN Amro bought Hungarian Credit Bank (MHB) and ING, another Dutch bank, bought Dunabank.

The National Bank of Hungary had got the ball rolling in 1989 by selling Tungsram, a light-bulb maker, to RZB, an Austrian bank. RZB quickly made a tidy profit by selling Tungsram to General Electric (GE). The Tungsram deal was "one of the most successful ever made in Hungary", says Mr Suranyi, who is now head of multinat-

ional banking at IntesaBNCI, an Italian banking group. It was a positive symbol of the whole privatisation process, he says. GE put in fresh capital and quadrupled the firm's light-bulb output in Hungary.

Jacek Siwicki, who was Poland's deputy minister of privatisation at the time, agrees there was a need to attract some big names, such as Pepsi, Goodyear and Henkel, rather than trying to sell shipyards and steel mills. The big names raised Poland's profile and showed investors we were "guys you could do business with", says Mr Siwicki, who now runs Enterprise Investors, the biggest private equity fund in Central Europe. Despite the problems, he marvels at how far his country has come.

But Poland was more cautious than Hungary about selling control of its banks to foreign investors. Although it floated bank shares on the stockmarket and sold minority stakes from 1997, the first majority bank stake it sold was in 1999: 50.1% of Bank Pekao to UniCredito of Italy. The upshot was that in the mid-1990s Polish banks had little access to new capital and western risk-management and IT systems. On the other hand bank shares were traded actively, which benefited the local stockmarket.

Now around 70% of Poland's banking sector is in foreign hands and the banks are moving towards western standards of service. But this was hardly part of the big bang that Leszek Balcerowicz, Poland's arch-reformer, inflicted on the rest of the economy. Today Mr Balcerowicz, who had two stints as finance minister (1989-91 and 1997-2000) and is now governor of the

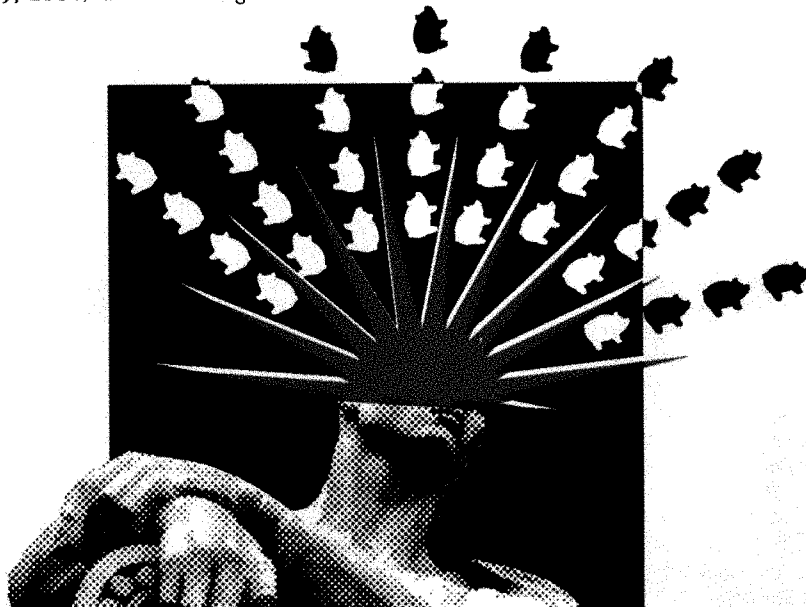
central bank, talks about the importance of radical and sustained reform and the need to build reliable financial institutions. But Poland, like almost every other country in transition, dragged out its banking crisis: it chose to bail out its banks in 1994 rather than cutting their ties to troubled enterprises.

The Czechs paid most heavily of all for botching the clean-up and privatisation of their banks, until the job was eventually done properly. "If you screw up your banking sector, the whole economy suffers," says Joanna James at Advent International, which invests private equity in Central Europe.

Unintended consequences

In 1997 the Czech government made a rather silly mistake that lost it control of a bank without putting it in safe hands. Investicni a Postovni Banka (IPB), the country's third-biggest, needed new capital. The government's National Property Fund, which owned 47% of the bank (and another 3% through an investment fund), inexplicably ducked the capital increase, so its stake was diluted. IPB, although a popular retail bank, had a bad reputation for buying political favours from both main parties. Technically it had now been privatised, but its balance sheet had not been cleaned up. When Nomura Securities, a Japanese investment bank, expressed interest in a minority share, it was hailed as the "western" strategic shareholder that would give IPB world status and credibility.

But when the bank needed more capi- ➤



tal, Nomura saw no reason to oblige. It had already made a tidy profit by selling two breweries owned by the bank and its investment funds to a South African buyer. It wanted the government to step in and make the bank saleable to a foreign buyer. In June 2000 there was a run on IPB, on rumours that it was about to report more losses. The government intervened on a Friday, sending in special forces sporting balaclavas and sten guns. Without time to organise a proper auction, and fearing a systemic banking crisis, the government decided to hand over IPB on the following Monday to Ceskoslovenska Obchodni Banka (CSOB), the best-run local bank, which had been sold to KBC of Belgium the previous year. It was a controversial and costly move that allowed CSOB to acquire another bank virtually risk-free. It could cherry-pick assets from the IPB portfolio and consign the rest to the bank consolidation agency, in exchange for government bonds.

This was the second time the government had ended up paying top dollar to get a bank off its hands. The first had been early in 2000 when it agreed to the sale of the biggest savings bank, Ceska Sporitelna, to Erste Bank of Austria. Sporitelna's existing loan book was ring-fenced: Erste and the government could pick the loans they wanted, and the rest went to the consolidation agency. But the government eventually learned its lesson. When it sold the last big bank, Komerčni Banka, to Société Générale last year, it insisted that the French bank buy the loan portfolio and the bank as a package deal.

Slovakia, which split away from the Czech Republic in 1993, did little to privatise its banks until 1998, when the xenophobic leadership of Vladimir Meciar came to an end. Six banks had collapsed in five years. The gross cost of restructuring the three biggest banks was the equivalent of 11% of GDP, according to Ivan Miklos, deputy prime minister for the economy. The net cost, after selling the banks and auctioning their bad loans, will be between 4% and 6% of GDP, he estimates. The buyers of the three banks were Erste of Austria (adding Slovenska Sporitelna to its sister savings bank in the Czech Republic), IntesaBCI of Italy and OTP of Hungary.

The war in the Balkans meant that only Slovenia, the smallest and least affected of the former Yugoslav republics, was able to establish strong links with western economies. It had a head start. Even under Yugoslav socialism, the Slovenes had close ties with western businesses. Many had

worked in Germany as guest workers; many of the brightest from other parts of Yugoslavia had settled in Slovenia as economic refugees. But Slovenia's size and its hostility to foreign influence meant that for years it resisted foreign capital as a solution for its banks and cash-starved industries. When Austrian and Italian banks two years ago were eyeing up the country's second-biggest bank, Nova Kreditna Banka Maribor, "there was such a stink from its citizens that the project was put on hold," says an American banker who was there at the time.

Slovenia's concern, beside a fear of re-colonisation by neighbours after only ten years as an independent country, was the stability of its currency in the face of large capital inflows or outflows. Grudgingly, under pressure from the European Union, the government allowed foreigners to buy minority stakes in banks. Société Générale bought a minority stake in SKB Bank and was later able to build a majority, which included taking over a 14.9% stake held by the EBRD. SanPaolo IMI, an Italian bank, bought a 62% stake (but with only 33% of the voting rights) in Banka Koper last year. The jewel is Nova Ljubljanska Banka (NLB), the country's biggest. "I would have bet my salary a year ago that this bank would never be privatised," says Murat Yildiran, the EBRD's representative in Ljubljana. But in May, KBC of Belgium won agreement to take a 34% stake, with the option of buying more over five years, though the sale still needs approval from the National Bank of Slovenia.

Serbia, less than two years into its reforms, has shut 23 banks, including four of its five biggest in January this year. Did it jump or was it pushed? The World Bank and others had plenty of advice for it. A World Bank survey on financial transition, published in July 2001, pointed clearly to the high cost of delaying bank reform. But taking the plunge still needed courage. Mladjan Dinkic, the governor of the National Bank of Yugoslavia, used a form of controlled bankruptcy to close the banks, giving plenty of warning to foreign inter-bank depositors to withdraw their money.

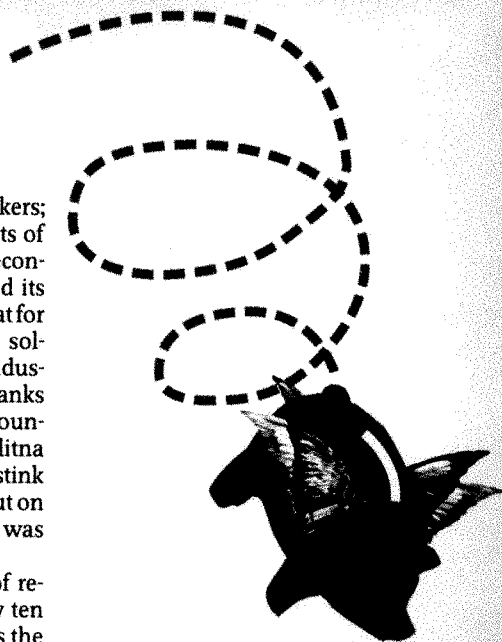
Unloved assets

Serbian investors were not sorry to see these banks go because Slobodan Milosevic, the then president, had seized their foreign-currency deposits to finance his wars in Bosnia and Kosovo, replacing them with near-worthless government bonds. The cost of the bank closures in January was about \$4 billion, the equivalent

of 1% of GDP, modest compared with similar moves in other Central European countries. Now the banks are being prepared for sale towards the end of the year.

"We paid a high political price for closing the banks," says Miroslav Labus, deputy prime minister in the Serbian government. "Now the banking sector is improving and savings are growing." He fails to mention the bank they did not close, Komercijalna Banka, which is popularly known as the "police" bank because of its closeness to the security forces: rumour has it that this bank was too sensitive even for Mr Dinkic to touch. But now it is a possible choice as a home-grown banking champion. "I would like to see two or three domestic banks competing with foreign banks, something like OTP in Hungary," says Mr Dinkic. OTP, Hungary's biggest bank, floated its shares on the stock exchange rather than acquire a foreign strategic investor.

Croatia, a war zone until the Dayton accords in 1995, spent the equivalent of around 22% of GDP rehabilitating its four biggest banks the following year. But there was a second banking crisis in 1998-99 when two big banks and several others became insolvent, costing another 5% of GDP to sort out. In April 2000 there was a run on Bank Istarska, which the government halted. It was time to look abroad for buyers. Within a year three big banks had been sold to foreigners—IntesaBCI and UniCredito of Italy, and Germany's Bayerische Landesbank. A British investment fund, Charlemagne Capital, also bought three banks. That put around 90% of Croatia's banking assets into foreign hands. More nimbly than other countries, Croatia was outsourcing the recapitalisation and to some extent the supervision of its banking sector. Thereby hangs a tale. ■



Rogue trader, rogue parent

Most of the banks in Central Europe have foreign owners. That is no guarantee that they will be well run

CENTRAL EUROPE has its own Nick Leeson or John Rusnak in the person of Eduard Nodilo, a dealer at Rijecka Banka, Croatia's third-biggest bank. Mr Leeson was the rogue trader who brought down Baring Brothers, a British merchant bank, in 1995; Mr Rusnak inflicted a \$690m loss on Allied Irish Banks earlier this year. Mr Nodilo, for his part, accumulated \$98m of foreign-exchange losses before they were discovered in February, wiping out the bank's capital. Like his western counterparts, Mr Nodilo had been hiding losses for several years. The market had noted that he was trading unusually high volumes, but the board of Rijecka Banka, when quizzed by regulators at the Croatian National Bank, said that everything was in order. Nor did Rijecka's parent, Bayerische Landesbank, ring the alarm bell—until it was too late.

So who was responsible? Bayerische Landesbank had bought the bank from the government two years earlier, which should have given it plenty of time to do due diligence. The bank had been valued by experts. The Croatian supervisors had overall responsibility to ensure the bank was properly run. But where there is a foreign parent, hard-pressed bank supervisors in Central Europe tend to rely on its

usually more rigorous controls. In Europe, at least, the parent's supervisor tends to look at the whole group, including foreign subsidiaries.

Even so, the fraud at Rijecka remained undiscovered for a surprisingly long time. When it came to light, Bayerische Landesbank did a rapid internal audit and decided to sell the bank back to the Croatian government for one kuna (about 14 US cents). By disposing of its purchase for next to nothing, the German bank had lost its capital stake of around \$70m. Even so, Cedo Maletic, a vice-governor of the Croatian National Bank, thinks it did not do enough: "Banks aren't shoes to be put in the garbage." Bayerische Landesbank does not owe Croatia anything, he says, "but if it wants to buy another bank here—no chance." Oddly, outside Croatia nobody took much notice of the bank's troubles.

Bayerische Landesbank owns another Central European bank, the Hungarian Foreign Trade Bank (MKB), in which it had bought a stake in 1994 and taken a majority in 1997. Through its affiliate, Bank für Arbeit und Wirtschaft (Bawag), it also has a stake in Istrobanka in Slovakia. Would it drop those too if they got into trouble? It argues that Rijecka was a special case—the fraud meant a time-bomb was lurking even before the government sold the bank.

aly, which owns banks in Hungary, Croatia and Slovakia. The Italian and Austrian parent banks in particular, having built a network of banks in the region, insist that they stand behind their subsidiaries.

The Rijecka case was a disappointment because Bayerische Landesbank was not prepared to back its subsidiary when it got into trouble. The German bank had problems at home, as the biggest creditor to the troubled Kirch media group. It was also alarmed by initial reports that the losses at Rijecka could be far bigger than they appeared, and that the entire bank was crooked. However, in May it managed to sell Rijecka Bank to Erste Bank of Austria for about \$55m.

Other retreats by strategic investors have been more understandable. Nomura Securities, which bought 40% of Investicni a Postovni Banka in the Czech Republic, was hailed at the time as a strategic investor. The Czech authorities even had a letter of intent from Nomura, undertaking to bring some expertise to the bank. But when IPB got into trouble, Nomura did not regard itself as responsible. After all, it is an investment bank. It was a lesson to the Czechs that they should find more appropriate strategic investors in future. They have done so with subsequent bank sales.

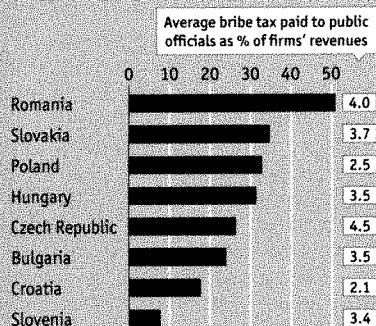
A handful of other foreign parent banks have been unlucky. Bankgesellschaft Berlin, in trouble because of its east German property portfolio, sold its Czech subsidiary, Zivnostenska Banka, to UniCredito of Italy in August. Kent Bank of Istanbul went bust in the Turkish banking crisis in 2001 and its Albanian subsidiary, National Commercial Bank, became the property of the Turkish government. That did not please Albanians, who had suffered Ottoman rule for centuries until 1913. Similarly, Demirbank in Romania was orphaned after its eponymous Turkish parent failed. It was bought by UniCredito. If subsidiary banks like these are well capitalised and properly supervised, there should be no problem finding another buyer if the parent gets into trouble. But the message to local supervisors is clear: they should not relinquish responsibility for the banks on their turf.

Polish supervisors are probably taking ►►

Back-hander index

Firms were asked to comment on the following statement: "It is common for firms in my line of business to pay some irregular unofficial payments to get things done".

% of firms bribing "frequently", "mostly" or "always"



*Response categories were: never, seldom, sometimes, frequently, mostly or always

Source: European Bank for Reconstruction and Development/World Bank survey, 1999

A better class of investor

Foreign banks that have taken majority or even minority stakes in Central European banks are known as "strategic" investors, which means something more than a portfolio investor who buys and sells bank shares. Local regulators assume that strategic investors have a commitment to their affiliate, and that they aim to apply the same standards of ethics, governance and risk management to it as they do at home. There have been a few disappointments, but most Central European regulators think that in general this has worked. György Suranyi, a former governor of the National Bank of Hungary, says a risk remains, and there is a need for tight supervision, but "the bulk of the responsibility lies with the strategic investor." He represents such an investor himself now, as head of multinational banking for IntesaBCCI of It-

► their strategic investors too much on trust. Several foreign-owned banks in Poland have a high level of non-performing loans—up to 60% in one instance—but a much lower level of loan-loss provisions. The shortfall tends to be guaranteed by the parent. “A lot of foreign banks don’t meet the standards,” says a local banker.

Second division

Several West European banks have shown real commitment to the region. Two Austrian banks, Erste Bank and Raiffeisen Bank, have become more Central European than Austrian. Erste owns the biggest savings banks in the Czech and Slovak Republics, employing nearly three times as many staff there as the parent does in Austria. It also has banks in Croatia and Hungary. Raiffeisen Bank owns Tatra Bank, reckoned to be the best private bank in Slovakia, and has subsidiaries in 12 other countries in the region. Other committed parents are KBC of Belgium, with CSOB in the Czech Republic and Slovakia, K&H in Hungary, Kredyt Bank in Poland and, subject to negotiation, 34% of Nova Ljubljanska Banka in Slovenia; UniCredito, with a big bank in Poland, Pekao SA, and others in

Bulgaria, Croatia, the Czech Republic, Slovakia and Romania; IntesaBCI, with banks in five countries in the region; and Société Générale with Komerční banka in the Czech Republic, and others in Bulgaria, Romania and Slovenia. Allied Irish Banks owns two banks in Poland, which it has merged. It landed in that country almost by accident, having offered technical assistance to one of the banks under a World Bank programme.

However, none of these parent banks is in the first league. Central Europe tends to be the stamping-ground of second-tier banks. Where are the Citibanks, J.P. Morgans and Deutsches? And where are the British, especially HSBC, that emerging-market specialist? True, Citibank bought the biggest Polish corporate bank, Bank Handlowy, in 2000, and has been present in Hungary for 16 years. But even Citibank, and certainly other top-tier banks, have not been punching their weight in Central Europe. Perhaps they are planning to wait for a few years and then buy one of the Austrians or Italians along with their Central European network.

HypoVereinsbank of Germany, though not in the big league, did exactly

that when it bought Bank Austria, which has a retail and investment-banking network in most Central European countries, having itself merged in 1997 with Creditanstalt of Austria, one of the pioneers of banking in Central Europe. ABN Amro, a Dutch bank, merged its Hungarian bank with one owned by KBC in a joint venture which is now under KBC management.

There will undoubtedly be further consolidation of banks in the region, either because their parents merge or because they sell out. According to Wojciech Kostrzewa, chief executive of BRE Bank in Poland, “You need a market share of 10-20% in markets which aren’t artificially regulated. Most banks here are too small.”

Mr Kostrzewa expects more departures like that of ABN Amro from Hungary (see box below). BRE Bank, the region’s only self-proclaimed indigenous investment

In and out

ABN Amro’s Central European excursions

ABN AMRO, a big Dutch bank, has a tradition of venturing into wild places in pursuit of customers. In the early days of post-communist transition it was everywhere. In 1996 it bought Hungarian Credit Bank (MHB), and invested a huge amount refurbishing its branches. Even in the smallest provincial branch, everything had to be done ABN Amro’s way, down to the office furniture imported from the Netherlands and expensive IBM hardware.

The management style too was imposed from Amsterdam, although the bank hired good local people. Accustomed to operating in former Dutch or British colonies, ABN Amro prefers to send out “soldiers” from head office.

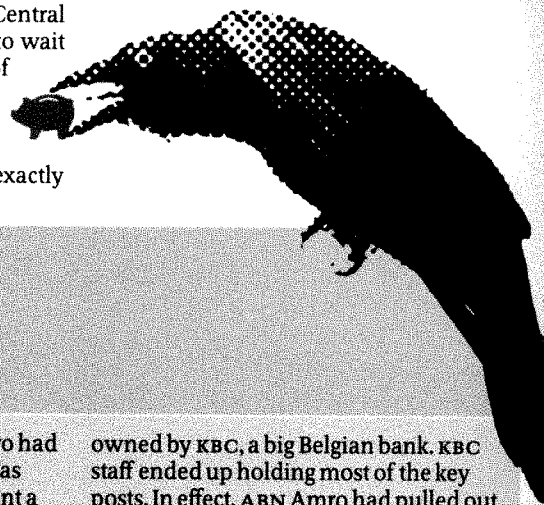
Whether those soldiers are good or bad, they usually stay for no more than three to five years, and are often preoccupied with office politics and promotion prospects back home.

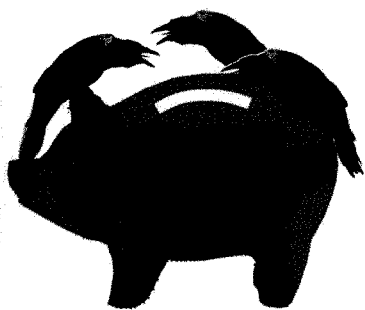
Despite this weakness, ABN Amro had an expanding business in Hungary, as well as in Poland, where in 1996 it sent a good Dutch soldier as country manager. He persuaded his bosses in Amsterdam that ABN Amro should buy a Polish bank. It had already looked at BPH, a medium-sized corporate bank in 1994, but balked at the price, and BPH was floated on the stock exchange the next year. By early 1998 ABN Amro was all fired up to buy it. But a change of management in Amsterdam and losses from financial crises in Russia and Brazil made it hesitate, and the Polish bank was snapped up by HypoVereinsbank of Germany. The blow to morale at ABN Amro in Warsaw has since caused key staff to leave.

Meanwhile, in Hungary, ABN Amro Magyar Bank lost money every year from 1995 to 2000, according to former staff. In July 2001 ABN Amro struck a deal to merge ABN Amro Magyar Bank with K&H,

owned by KBC, a big Belgian bank. KBC staff ended up holding most of the key posts. In effect, ABN Amro had pulled out of Hungary.

Observers think ABN Amro may have been a victim of its own successful recruitment. Among its alumni is Zsigmond Jarai, a former finance minister and now the president of the National Bank of Hungary. The current finance minister, Csaba Laszlo, managed the merger between ABN Amro’s bank and K&H. Another former ABN Amro manager is now chef de cabinet to the prime minister, Peter Medgyessy. Two of the bank’s senior expatriate managers moved to Citibank and Raiffeisen Bank respectively. Another Hungarian alumnus runs Raiffeisen Bank in Belgrade. ABN Amro seems to have played an important part in the development of Central European banking without getting much of either the benefit or the credit.





► bank, expects to be involved as a deal-maker. BRE Bank is 50% owned by Commerzbank, one of Germany's universal banks. It is involved in some Polish industrial workouts, such as bankrupt Elektrim, which is feared to be eating into its risk ratios. Would Commerzbank stand behind BRE? Eyebrows have been raised in the banking community at BRE's readiness to take equity stakes in companies, while funding itself with short-term retail deposits. "He's running his bank like a hedge fund," says a local investment manager of Mr Kostrzewa. But auditors and supervisors seem happy, one even calling BRE "the best-run bank in the country". The risk ratios look all right, say correspondent banks grudgingly. Mr Kostrzewa complains that he is singled out because no other bank is taking equity risk. He sings the praises of the British merchant banks of yesteryear, and of Mediobanca, which restructured corporate Italy in the 1950s and 1960s.

Croatian supervisors are less than delighted by the presence of Charlemagne

Capital, a British-based manager of equity funds, which has been able to build up and control a considerable banking group in Croatia. Charlemagne, until last year known as Regent Europe, bought its first two Croatian banks, Dalmatinska Banka and Istarska Banka, in 2000 from the government's bank rehabilitation fund. The national bank supervisors had no control over the sale. Charlemagne has since added another regional bank and will merge them all, moving the headquarters to Zagreb and calling it Nova Banka.

Charlemagne has no obvious banking expertise, apart from a similar control of Hebros Bank in Bulgaria. Alarming, after buying the Croatian banks it stopped their operations for a while, which cannot have been good for business. Charlemagne's declared strategy is to improve the banks and resell them in three to seven years. Meanwhile it is bidding for another Bulgarian bank, Biochim.

Taking the rough with the smooth

Foreign non-banks may not be the ideal parents for Central European banks in transition, but then countries cannot always be too choosy. The first bank that Hungary sold control of was Budapest Bank, in 1996, to GE Capital. "The deal was badly structured and included political involvement," recalls someone close to the

sale. The new owners severely reduced the bank's product range and turned it into little more than a consumer finance house. GE Capital is reckoned to have made plenty of money, but it did not shower the market with new products and credit cards, as the sellers had hoped.

The EBRD has invested in the equity of more than 80 banks in transition countries, usually accompanying a foreign strategic investor. It sees this as a vital part of its job, although it has had to be pragmatic about some of its business partners. "If we don't like what we see, we just withdraw from the board," says Kurt Geiger, director of the financial-institutions group at the EBRD. In many cases it has sold its stake once the bank is on a steady path.

For the time being these banks, answerable to foreign parents, are the dominant source of finance in these economies. That is not strictly healthy. Debt financing can be fickle in times of trouble. Foreign owners may suddenly lose interest in the local economy and decide to put their resources elsewhere.

For now, these countries are relying too heavily on these foreign-owned banks to provide their working capital. In principle, local sources of capital—securities markets, pension funds, insurance companies—are available. But as yet they do not offer a real alternative to the banks. ■

Capital punishment

WOOD & COMPANY claims to be Prague's biggest equity broker. It used to be even bigger, boasting offices in Poland, Hungary, Slovakia and Ukraine as well as in London and Istanbul, but that was before equities had felt the full effect of the Russia crisis of August 1998, which sent a shock through capital markets around the world. Now Wood has shrunk to two locations, Prague and Bratislava, although it still does some cross-border business. Richard Wood, the founder, has long since moved on.

Most stockmarkets around Central Europe are dying. In Prague, there has not been an initial public offering (IPO) of shares since the 1930s, even though thousands of companies were listed in the 1990s during the mass privatisations. The Czech stockmarket is not a place to raise

new capital. Over 100 companies are still listed, but only a handful are actively traded, none of them blue-chip names.

Hungary's stockmarket is marginally better. It does have some blue chips, such as Mol, an oil company, Matav, a telecom company, and OTP, the country's biggest bank. It has even had some proper IPOs, though the last one, of Synergon Information Systems, was in 1999. Volumes are still desperately low. "I'm afraid Hungary will go the way of the Czech Republic," says Petr Koblic, chief executive in Prague of CAIB, the investment bank of the German HVB group.

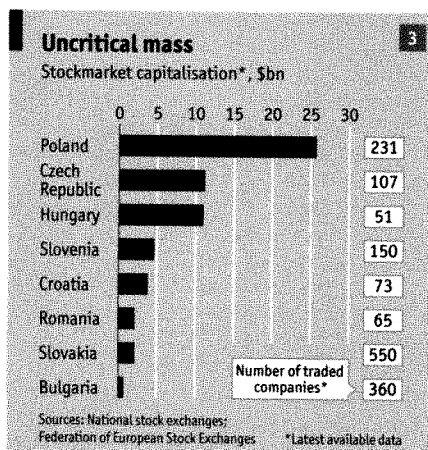
In Belgrade the technocrats—some of them former bond traders at Wall Street firms—have decided, sensibly, that equity markets must wait until Serbian companies have become more transparent.

Troubled local stockmarkets are looking west for allies. Many of them will not survive

Meanwhile, they are building a government bond market. A corporate bond market may follow.

Arguably, the only equity market in the region that is big enough to be sustainable is Poland. The Warsaw Stock Exchange has a market capitalisation of around \$26 billion, more than all the neighbouring stockmarkets combined. With a population of nearly 40m, Poland would expect to have bigger companies, bigger investment institutions and a bigger number of retail investors than its neighbours. Romania, the next most populous country in the region, with around 22m, should be able to sustain a national stockmarket too, but it is a long way behind Poland, Hungary and the Czech Republic.

And even in Poland, there are doubts whether a national stock exchange can ►►



► survive European consolidation. Turnover has dwindled to \$25m a day. Belgium, France and the Netherlands have already merged their stockmarkets to create Euronext. The Warsaw Stock Exchange has signed a cross-marketing agreement with Euronext, but has made no commitment to join up. Being 98% owned by the Polish treasury, it cannot take such a decision on its own. But by the end of this year Wiesław Rozlucki, chief executive of the exchange, should be able to agree with the treasury on whether to look for a strategic partner, or whether to slug it out alone. There have been proposals for a regional exchange based in one of the bigger countries, but Mr Rozlucki thinks that is a bad idea. The market would lack critical mass, he claims, pointing to Vienna's attempt to become a hub for Central European stocks. A Viennese exchange, Newex, aimed at regional companies, was actually traded electronically in Frankfurt—and proved a failure: it has just been absorbed by the Frankfurt exchange.

Great expectations

Perhaps too much was expected of Central Europe's fledgling stock exchanges. An American agency, US Aid, spent millions of dollars on projects to establish capital markets in a post-communist wasteland. But setting up a stock exchange is one thing; creating the necessary conditions for an active equity market quite another.

A healthy stockmarket needs transparent reporting by companies, good corporate governance and a respect for shareholders' rights. Those conditions often lag a long way behind the launch of share trading. Second, it has to have a domestic investor base. Too often, nascent stockmarkets have attracted a flood of speculative investment from abroad, only to see it

disappear at the first hint of trouble. The obvious answer is to build a class of institutional investors, starting with pension funds, and to encourage mutual funds and private portfolio investors. Third, listing on an exchange must be attractive to companies. Many smaller businesses are deterred by the cost and the disclosure requirements. Fourth, the underlying economy should have a track record of reasonable stability. In many countries a flurry of equity mania in the early 1990s was followed by high inflation and a stock-market bubble which severely damaged the value of investments.

Poland is ahead in the game because it avoided a market bubble, and took trouble to build up pension funds. Since 1999 all employees born before 1969 have been obliged to contribute 9% of their salary, of which a portion goes into private pension funds. That has produced funds totalling around \$6 billion so far. Some 40% of that money can be put into equities, of which 5% may be invested abroad. That gives the Polish market a predictable expansion of its equity base, encouraging other investors to come in too.

Hungary reformed its pension system in 1998, but its pension funds are growing only slowly in a thin equity market. Many companies were sold to foreign investors rather than being listed on the Budapest Stock Exchange. However, there were some landmark IPOs, starting with Danubius in 1992. The government also chose to list Mol and OTP rather than sell stakes to strategic investors.

The Czech Republic, having seen many privatised companies delist for lack of investor interest, might be able to revive enthusiasm by floating a small equity slice of companies it has privatised recently. Erste Bank of Austria, having completed its takeover of Ceska Sporitelna, the big local savings bank, had to delist the stock, but intends to fill some of the gap by issuing its own shares on the Prague market in October. Traders are sceptical that this will add much liquidity locally. Share trading will gravitate to the market where a company's shares are most heavily traded. Although the region's blue chips, such as Mol and Poland's KGHM, are listed in London or Luxembourg, the share price is still determined locally and most of the trading is done on the spot.

However, because of the consolidation of exchanges in Europe, and the growing share of institutional trading, Central European exchanges will be increasingly isolated unless they have links into the West.

Mr Rozlucki at the Warsaw Stock Exchange accepts that Poland's blue chips may migrate to a multinational exchange, and that Warsaw should be part of a wider structure. But for small and medium-sized companies, he believes disclosure of corporate information, price discovery and the surveillance of companies and brokers will stay closer to home. The Warsaw exchange is in with a fighting chance "if we can provide alternative sources of capital", says Mr Rozlucki.

Local attractions

Jan Sykora, a partner at Wood & Company, believes there will be a role for local regulators as "gatekeepers to the global market". But he is sceptical whether, eventually, local listings will work "when there's so much consolidation of asset managers and investors". Warsaw may retain more local interest, but on the Prague exchange 99.5% of the trading volume is institutional orders and 95% of those are from abroad, says Mr Koblic at CAIB. Slightly more promising is the Czech Republic's corporate bond market, which is bigger than Hungary's, Poland's and even Spain's (see table 4). But it reflects the fact that Czech companies have great difficulty raising bank loans: in 1999-2000 they repaid more to local banks than they borrowed.

One thing that would help the region's stock exchanges is progress on corporate governance. Shareholders' rights continue to be abused. An inadequate legal system means that redress takes years, so most people do not pursue cases. A company's management "can still present an illegal action to shareholders and get away with it", says an investment banker in Prague.

The worst abuses of the early days involved companies and the government-inspired national investment funds stripping out assets under shareholders' noses—"tunnelling", as it was called. Another common peccadillo was for strategic investors to pay a premium for a control- ►

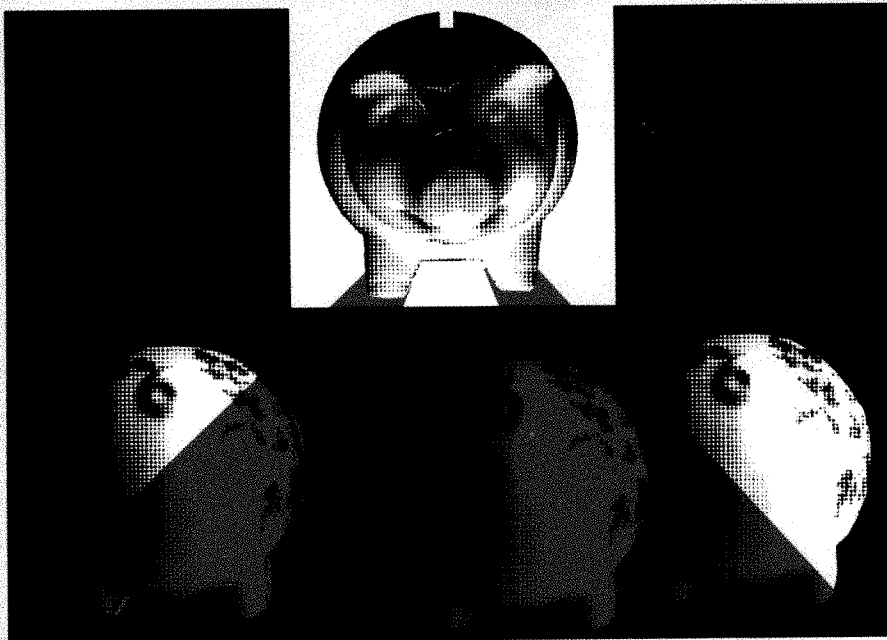
Backward bond markets

Outstanding domestic debt securities as % of GDP end 2000

	Financial	Corporate	Total*
Germany	49.7	1.3	90.2
Portugal	16.1	9.6	61.7
Spain	5.3	4.8	59.0
Czech Rep.	5.5	5.3	46.1
Hungary	na	1.5	35.5
Poland	na	0.0	20.3

Source: European Investment Bank

*Includes public bonds



ling stake in a company without making a general offer to shareholders. Mol, the Hungarian oil company, did this when taking over Slovnaft, its counterpart in Slovakia. "At that time no full bid was required," parries Zoltan Aldott, head of strategy at Mol, and also a board member of the Budapest Stock Exchange. "If we increase our stake now, we will make a public offer."

Would you do this at home?

HypoVereinsbank, a German bank, paid the Polish treasury more than twice as much per share for Bank Przemyslowo-Handlowy (BPH) than it paid minority shareholders. ING, a Dutch bank, took a majority stake in Bank Slaski, another Polish bank, then made huge provisions on the balance sheet, depressing the share price before buying out the minority shareholders. These foreign companies were taking advantage of lax local regulation to do things they could not get away with in their home countries.

Poland now has two committees working on corporate governance. In Romania the chief executive of the Bucharest stock exchange, Sergiu Oprescu, has started a new category of listing for super-compliant companies, called the "transparency-plus tier". Two have applied, but so far neither has achieved the upgrade.

Raimondo Eggink, a Dutchman, led the first legal challenge by minority shareholders in Poland, against Michelin of France for unfairly transferring profits from its listed local subsidiary, Stomil Olsztyn. In 1999, he also sued a Polish company for paying a premium to shareholders with a stake of more than 1% when it delisted its stock. In fact, the company was acting within the law, but Mr Eggink claims that the law in question is unconstitutional. The case has been in the High

Court for a year and a half. "If it's thrown out, I'll take it to the Constitutional Court," he says stoically. "I'm doing it for fun." He is paying his own legal costs, which so far have been modest. It seems that Mr Eggink's activism has won sympathy in high places: the treasury recently made him a member of the supervisory board of the stock exchange.

Perhaps it was too much to expect Central European countries to develop mature and properly regulated securities markets within a few years when it took centuries to develop them in the West; and given the poor examples of corporate governance offered by Enron and a growing list of other western companies, it seems that even mature markets are no guarantee against abuse. But there is an alternative way to encourage an equity culture in the region: direct private investment in unlisted companies.

Horizonte Venture Management, a small private equity firm in Slovenia, has had two investment failures. In the first, it backed a company that had no international market for its product. The second was due to a scam: a Slovenian firm it invested in bought overpriced, inappropriate machinery from an Austrian entrepreneur, which he had found second-hand in the Czech Republic. But apart from those, Horizonte has done well, venturing first into Slovenia, then Bosnia & Herzegovina and finally Croatia. In 1992, when Slovenia was only a year old and its continued independence looked shaky, Horizonte was having trouble raising money for a Slovenian fund. A Dutchman at IBM's pension fund came to the rescue. He had been to Slovenia and judged that it was already the best-run economy in Central and Eastern Europe.

Private equity can enter these new market economies early because it requires little infrastructure—just an agreement be-

tween investor and entrepreneur. If the investor has found the right person the business grows, and within three to seven years it is sold to an acquisitive company, or listed on the local stock exchange.

A lot can go wrong, and hand-holding is essential. The entrepreneur may need help with developing foreign markets, raising fresh capital or taking out patents to protect his product. A hands-on private equity firm like Horizonte gets involved at this working level, as well as trying to ensure the company is run according to standards the investors demand. Apart from good corporate governance, the usual stipulation is no drugs, no arms and no prostitution. As it happens, a drug company of the legal kind is one of Horizonte's most promising Slovenian investments: Transcell, a pharmaceutical firm with ambitions to become a world leader in the treatment of tumours.

Serial entrepreneurs

The challenge for private-equity investment firms is to find a certain kind of entrepreneur who is skilled at building up a business, but not set on preserving it as a family heirloom. "Private equity breeds a class of serial entrepreneur," says Pierre Mellinger, who runs AIG-CET Capital Management (Poland) in Warsaw. As yet, those entrepreneurs cannot be too picky about their source of funding in the region. In essence, their choices are to find the finance themselves, take a bank loan or team up with a private equity investor. The leadership provided by this new class of entrepreneur is very important for an economy, says Kurt Geiger at the EBRD.

Poland is the most popular place for private equity investment because it has the biggest population, but that may be short-sighted. Miroljub Labus, the deputy prime minister of Serbia, is striving for a customs union of those Central European countries at the back of the queue for EU accession. This should create a bigger internal market and attract more foreign direct investment, he argues. But finding good managers is a challenge, and anyone over 45 is usually too set in the nannyish ways of central planning to run a competitive business. "We need a new breed of people who will take the risk of making decisions," says Dan Pascariu, who used to run the Romanian Foreign Trade Bank and now heads a German bank subsidiary, HVB, in Bucharest. "We all carry too much baggage; the 26-year-olds don't."

The EBRD has invested in more than 80 private equity funds over ten years and has made about 800 separate investments. To ►►

have the bank on board is good for marketing one's fund, says Piotr Bardadin, who runs Renaissance Partners in Warsaw, and investors like its insistence on high environmental standards. The EBRD has found that the bigger funds tend to do best, perhaps because they have more resources for doing due diligence and carry more clout with host governments and with the companies they invest in. The EBRD's internal rate of return on its investment in these funds is in the high teens, says Mr Geiger. It has its own equity portfolio too, much of it invested in banks. Apart from a few bank failures in Russia, Estonia and Latvia, the banking portfolio has done well, providing the EBRD with an internal rate of return of around 20% a year since its first investment in 1992.

Enterprise Investors (EI), based in Warsaw, is the biggest and earliest private equity manager in the region, with around \$4 billion-5 billion under management. Its

boss, Jacek Siwicki, was at the privatisation ministry in the heady days of mass privatisation. EI's charter allows it to invest 30% of its funds outside Poland. It has made investments in Romania and Slovakia. Mr Siwicki thinks that private equity in Central Europe is not that far behind practice in the EU or even North America, where private equity funds started in the 1970s. The challenge is to find an exit, given that even the Warsaw Stock Exchange is not a great place for IPOs (although EI recently floated a jewellery business for about \$4m). The company has recently done well with sales to strategic investors: it sold a small-business bank to Fortis and a mortgage bank to GE Capital.

Private equity is not always the best tool. There is room for other kinds of venture capital in the region, for entrepreneurs or business owners who do not want to give up equity. The EBRD has teamed up

with Mezzanine Management to launch a fund for mezzanine finance—development capital in the form of high-yield debt, often with some equity characteristics. Accession Mezzanine Capital, with €75m in its kitty, is aimed not at entrepreneurs directly, but at private equity funds dealing with entrepreneurs who want to keep their business.

During a decade of assisting transition in Central Europe, development agencies such as the EBRD, the World Bank, the European Investment Bank and Kreditanstalt für Wiederaufbau have increasingly concentrated on helping small businesses get bigger. Now even those banks that started off by financing corporate giants and masterminding mergers and acquisitions have turned their sights to small and medium-sized enterprises. That can only be good for those who want to start their own business. ■

Back to nursery school

THIS is how a small business died. Fifteen years ago, Aniko, a blonde, feisty mother of two, worked for one of Hungary's centralised foreign trade organisations (FTOs), selling honey to Western Europe. She was one of the privileged few who travelled to trade fairs and socialised with foreign buyers. When the FTO closed in 1991, she was left jobless and began to sell honey herself, using her contacts with beekeepers and foreign clients. But she needed finance to bridge the gap between buying the honey and getting paid herself. One Hungarian bank obliged, charging interest at 37.5% and taking the family house as collateral. Business improved, interest rates came down and Aniko had a nice little earner—until 1999, when the EU began to dismantle its tariffs on agricultural imports from Central Europe. The duty on Hungarian honey was cut from 16% to 10%. But, rather unfairly, the duty on Czech, Slovak and Romanian honey went down from 16% to zero.

Hungary's beekeepers protested. If only they had kept their mouths shut. Their protests alerted the banks, which decided they could no longer lend to the honey trade while Hungary had "this international honey problem". Aniko's bank, K&H, a Hungarian subsidiary of KBC

of Belgium, refused to provide finance, even when she produced a firm order from a loyal German buyer. Unfortunately she had already spent the 16m forints (\$63,000) she would have made on the German deal, so she had to let down the beekeepers, close the business and remortgage her house. Now she is selling honey again, but on 2% commission.

Of course every bank must stick to its credit policy. There may have been good reasons why K&H could not lend. But undoubtedly many small businesses are being starved of finance in Hungary, Poland, Slovakia and elsewhere, simply because they do not meet inflexible credit criteria.

In Serbia, the surviving banks—after the closure of 23 in the past year—are awash with deposits, but they are not inclined to lend to small businesses, says Mladjan Dinkic, governor of the central bank. "One reason is the potential risk, but they also don't have the skills to evaluate credit." The same is true of most banks in the region, although their foreign strategic partners are beginning to change that. The danger is that credit-point-scoring systems of the sort used by banks in the West are too crude to fit individual circumstances.

Nursing small and medium-sized enterprises (SMEs) in Central Europe to create a

Small-business finance is at last beginning to get the attention it deserves

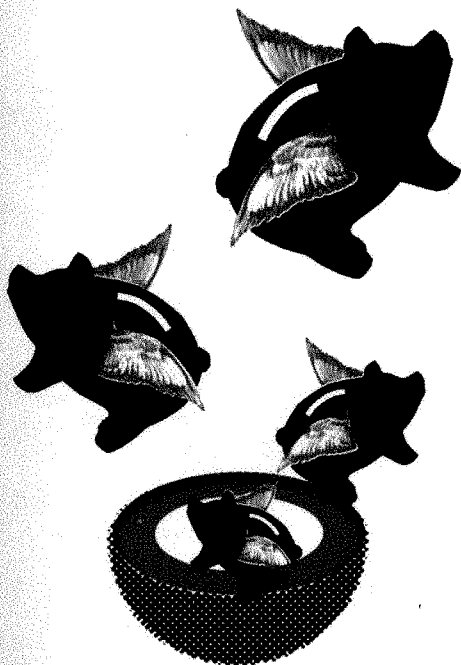
Starter packs

Micro-and small lending, April 2002

Project	Amount of loans outstanding \$m	Arrears >30 days, % of loans outstanding
Albania FEFAD Bank	15.4	3.44
Bosnia MEB	19.2	0.92
Bulgaria Procredit	10.9	0.00
Kosovo MEB Kosovo	11.6	0.16
Romania Romania MFI	5.8	0.75
Russia RSBF	156.5	0.81
Yugoslavia MFB	10.9	0.30

Source: European Bank for Reconstruction and Development

much-needed *Mittelstand* is still too labour-intensive to be profitable: it needs technical assistance and some subsidy. Some help has been forthcoming from America, not least because of a perceived need to keep Central Europe onside: after all, much of it is run by retooled former communists. In 1989 America's Congress voted to set up the Polish-American Enterprise Fund, which pioneered the development of smaller businesses in the region. By 1994 it had invested around \$200m. It was followed by the Russia Small Business Fund, and similar funds for Bulgaria, Ro- ➤



mania and countries in the Caucasus. When America's treasury secretary, Paul O'Neill, attended the EBRD's annual meeting in Bucharest in May, he made a point of visiting a small furniture factory nearby that had been given a small-business loan.

Even the countries in the first wave of EU accession need more small-business finance. But Peter Felcsuti, managing director at Raiffeisen Bank Hungary, warns against a one-size-fits-all concept for the region: "In Poland, a company with €5m in sales is treated as an SME, whereas in Hungary, because of the competition between banks, even a €2m company can get special service as a corporate borrower."

The EU's Phare programme channels funds into small-business lending via the EBRD and other European financial institutions. Without the right incentives the banks can suddenly pull the plug. The EBRD's programme, which started at the end of last year, opens lines of credit to local banks that sign up. The EU pays for technical assistance. There are grants to help with such things as marketing and training loan officers. The maximum loan is €250,000, and the average around €25,000, but two-thirds of the total number are micro-loans—anything from \$50 to \$10,000. There is an incentive scheme for the banks: if their portfolio performs well, they get a funding subsidy of 3.4-5.5% from the EU, depending on the size of the loan. "Our biggest concern," says Charlotte Ruhe, who runs the EU-sponsored scheme at the EBRD, "is that the subsidy should not be passed on to the borrower. That would distort competition."

So far the EBRD has signed up 23 banks

in the ten accession countries. About €180m has been lent. More important, the average response time for applications from borrowers has come down from a month to five days. The most enthusiastic bank, says Ms Ruhe, is Bank Zachodni WBK in Poland, whose management is committed to the project and has trained loan officers in 300 branches. In the Czech Republic, experts from Shorebank, a small-business bank in the Chicago region, are helping Ceska Sporitelna run its SME lending programme. The bank tried to expand into small-business lending ten years ago, with disastrous results: it had to be bailed out. But under its new owner, Erste Bank of Austria, it is now flush with deposits and trying to broaden its loan portfolio.

Although securing loans is important, "we try not to turn down a loan that is not based on collateral," says Greta Larson, a Shorebank expert working at Ceska Sporitelna. Recently the Czech Republic amended the law to permit a lien on movable collateral such as machinery and other capital goods. Neighbouring Slovakia has also passed a new law, based on American practice, which from January 2003 will allow machines, cars, furniture and even intellectual property to be used as collateral. That puts it ahead of most European countries using Napoleonic law, says Katarina Mathernova, an adviser to the government.

The European Investment Bank (EIB) also assists small business through its "global" loans. Unlike the EBRD, which adds technical assistance and monitors each project locally, the EIB tends to push out the money from its headquarters in Luxembourg and trust the local banks to run the projects. As a safeguard, it usually chooses banks whose shareholders include the EBRD, the International Finance Corporation (an affiliate of the World Bank) or Kreditanstalt für Wiederaufbau (KfW), or it lends through the central bank, with a sovereign guarantee. KfW also has a programme of its own, which is slightly cheaper than the EBRD's. The EIB undercuts them both.

Think small

When Elizabeth Wallace was working for the EBRD in the early 1990s, she was struck by the wastefulness of closing down big chunks of the communist world's arms industry without helping the newly unemployed to start new businesses. The EBRD's minimum loan in those days was \$15m. An out-of-work munitions worker might have needed a loan of \$10,000 to start

growing mushrooms in the factory where he once made bombs, says Ms Wallace. Another \$10,000 could have started a business cutting up redundant battle tanks. Yet none of this was being done.

Against opposition within the EBRD, notably from Ronald Freeman, the vice-president, Ms Wallace—who is now director for small-business finance at the bank—raised \$150m from G7 governments to start the Russia Small Business Fund. Pilot projects in Russia were successful. Losses have been minimal: during the 1998 crisis, when the government defaulted on its debt, "we lost some banks [which went bust] but we kept the clients," Ms Wallace says. One good thing about micro-loans is that the mafia, which to varying degrees is active throughout Central and Eastern Europe, is not interested in taking a cut of such small-scale business.

The EBRD's micro-lending programme, which is now well-established, channels lines of credit to local banks specially set up for the purpose. To date the bank has mobilised \$500m of small loans to the region. There are micro-lending banks in Albania, Bosnia, Kosovo, Moldova, Russia and some Central Asian countries. The performance of these banks depends almost entirely on the quality of the loan officers, who must identify good potential borrowers, understand their psychology and keep them motivated.

Collateral is the stumbling-block for most small-business lending. What can a borrower pledge when starting from zero? Ms Wallace's team sought advice from the World Bank and from micro-banks in Indonesia, Mozambique and elsewhere, and found that almost anything will serve as collateral, provided it means a lot to the borrower. It could be a cat, a cow or a treasured fur coat, but preferably a house. As long as the borrower is determined to hold on to the collateral, he or she will probably go on servicing the debt. In most countries the arrears rate has been remarkably low, under 1%. Even in Albania, where a pyramid scam hit thousands of people, the arrears amount to only 3.4% (see chart 5, previous page). The Micro-Enterprise Bank in Kosovo is thought to be the most profitable in Central and Eastern Europe.

In the 1990s many international banks were trying to reduce their loan books and concentrate on fee income from corporate finance and the more affluent clients. Now some have decided that they were wrong to neglect retail and small-business lending. That should make life easier for small borrowers like Aniko. ■

Inconspicuous consumption

PETER KISBENEDEK used to sell insurance. Before that he was in white goods. Perhaps he is just the man to bring a fresh approach to retail banking in Hungary. Austria's Erste Bank must have thought so, because it hired him in 2000 to run its small bank there.

Small, but getting bigger. Erste had bought three small Hungarian banks in the late 1990s and merged them under its own name. At the end of 2000 it had around 1.8% of the retail market. Mr Kisbenedek saw a gap in the provision of mortgages and sold them hard. He is convinced the mortgage market will grow, and Erste Bank with it. By April 2002, Erste reckoned its share of the retail lending market in Hungary had grown to 4.3%.

It also opened lots of new branches on the cheap—ten in Budapest last year, at an average cost of €200,000 a time. Even no-frills Erste used to spend ten times that on opening a full-service branch. Most of the new branches are in shopping malls, where the infrastructure is already in place, and each has a staff of only four, all of them salesmen. Credit decisions and processing are handled centrally. The bank is prepared to close branches that do not work—“like shoe shops”, says Mr Kisbenedek. By the end of 2002 Erste plans to have 35 branches in Budapest and other big cities, and will be storming towards the 20-25% share in retail banking and 8% share in small-business lending that it believes it needs to become a force in Hungary. To get there faster, it will probably try to buy another bank.

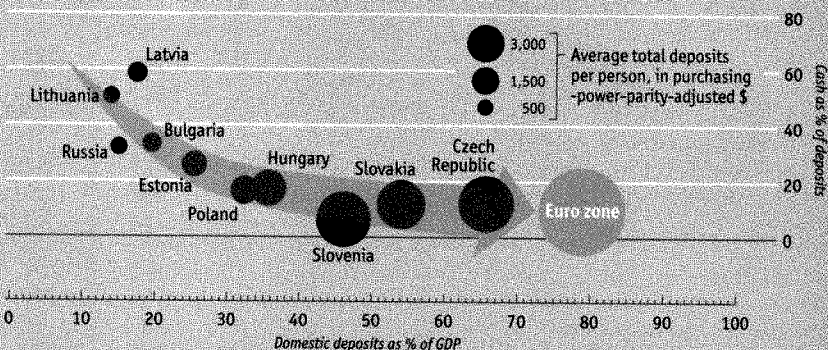
But the retail market in Hungary is getting cluttered. Even banks that previously had no interest in this particular sector now see the attractions of a sophisticated and increasingly affluent clientele. They include Citibank, Raiffeisen Bank and Central-European International Bank (CIB), which previously concentrated on corporate banking. The retail market is already the stamping-ground of Postabank, Budapest Bank (owned by GE Capital), K&H Bank (owned by KBC) and HVB Bank of Germany, all dominated by OTP, the big savings bank, “like Snow White and the seven dwarves”, says a competitor.

Erste is going for a market share of

Suddenly everyone wants to harness the power of consumers. But they are still thin on the ground

Migration from a cash economy

Mid-1999



Source: "Financial Deepening and the Role of Financial Crises", by Stephen Peachey and Alan Roe

above 20% in several Central European countries. In the Czech Republic and Slovakia it has two sister savings banks, Ceska Sporitelna and Slovenska Sporitelna, which are already market leaders. In Croatia, adding Rijeka Bank to the three banks it has already bought and merged should bring it close to a 10% share. Several other European banks, mainly Austrian and Italian, have similar plans for the region.

This is in marked contrast to European banks' strategies for the euro zone, where cross-border bank mergers have so far been rare. Is there some reason why a retail presence straddling several countries should work better in Central than in Western Europe?

Certainly the market is less mature. For retail financial services, Central Europe is almost virgin territory. Mortgages are only one of the products that have started from scratch. Others include leasing, credit and debit cards, asset management, securities broking, pensions and insurance. Ownership of private property is still underdeveloped in Poland, compared with countries such as America or Britain, says Pierre Mellinger at AIG-CET in Warsaw. The Poles mostly keep their wealth in disposable assets such as cars.

Until that changes, building up capital markets and investment products there will be difficult. Improvements to legal systems and bankruptcy procedures would help, by providing more incentives for

private and corporate borrowers to repay their debts. It would unlock chains of inter-company debt, as well as weaning banks off the easy option of keeping big chunks of their balance sheet in (supposedly) risk-free government bonds and encouraging them to take more credit risk. "If small-business lenders are experiencing only 1% of bad debts, it seems to me the banks aren't taking enough risk," says Paul Cunningham, a partner at PricewaterhouseCoopers in Prague.

The banks operating in former Yugoslavia face a special challenge. Companies there have been able to make their payments via a central system called Zop where they keep their accounts. Until Zop is dismantled, it will remain hard for banks to build an account relationship with corporate customers.

Under the mattress

Banks in Croatia, Slovenia, Serbia and a number of other countries had a one-time chance to gain more customers towards the end of 2001, just before the introduction of euro notes and coins, when thousands of accounts were opened to convert D-marks into euros. Much of this money had been sitting in shoe-boxes and under mattresses for years. According to one estimate, a total of €4 billion-8 billion was converted and deposited in Serbian banks, but most of it was whipped out again soon after January 1st. Raiffeisen Bank's three

► branches in Serbia took around €83m of extra deposits during that period. In Croatia, banking assets reported at the end of the year had grown by 33%, "mainly because of the euro conversion," says Ljubinko Jankov, head of research at the Croatian National Bank.

It is reassuring that there is this extra wealth lurking under mattresses. But in Serbia, for instance, it means that there may be up to €8 billion lying idle and not working for the economy. Foreign-owned banks have been better at making such one-time deposits stick. Raiffeisen suffered no net outflows, and attracted more deposits until the May 31st deadline.

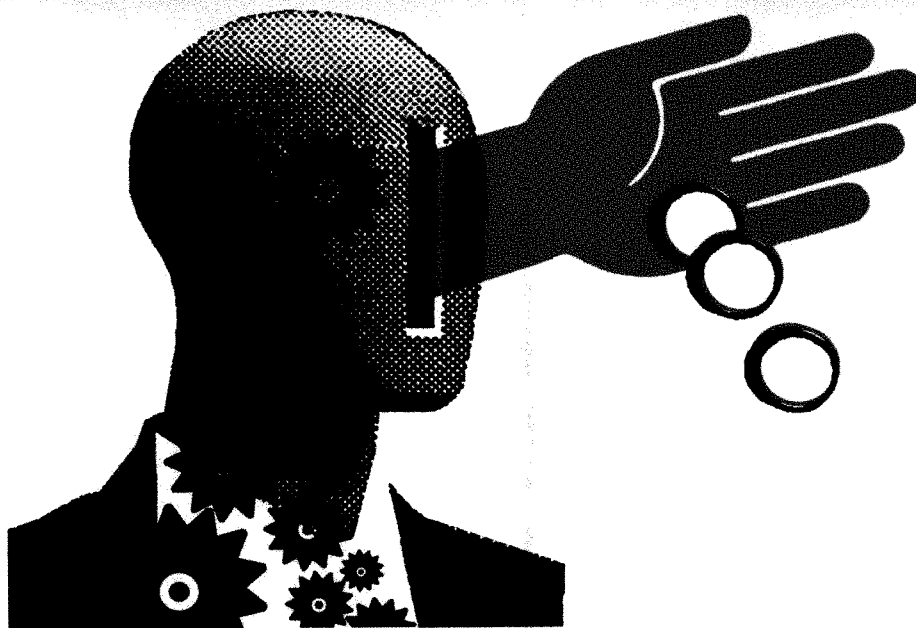
A study by the EBRD on bank reform, looking at 515 banks in 16 transition countries, shows that reform does not necessarily increase lending to customers. Often the government bond market takes precedence, crowding out private borrowers.

In the Czech Republic, Slovakia, Hungary, Bulgaria and Macedonia, the ratio of domestic credit to GDP is between 68% and 103%. Everywhere bar Slovakia, it is well below the ratio found in other market economies at a comparable stage of development. Worryingly, in Poland, Croatia and even the highly westernised Slovenia the ratio is below 40%. At the present rate of asset growth, it would take Poland 141 years to reach a level appropriate for a market economy, according to the EBRD.

The study suggests that foreign-owned banks are no better at beefing up their loan books than state-owned banks or locally owned private banks, but their cost-effectiveness and productivity are higher. In general the presence of foreign banks, or banks with strategic foreign partners, appears to have increased competition and brought down charges.

Looking ahead

In another ten years, the banks that are beginning to dominate the region will probably have been acquired by larger international financial groups like Citigroup, Société Générale or Goldman Sachs—perhaps even Axa or Aviva. By that time, most Central European countries will be using the euro and will have become part of a vast financial market akin to that of the United States. There will be continent-wide brands of consumer finance and also, with luck, sources of finance for local small business. Shares in the major companies will trade only in the big centres, such as London, Paris and Frankfurt, but many more people in Central Europe will take their savings out from under the mat-



tress and put them to work in the financial markets, whether in bonds, shares, private pensions or mutual funds. Their countries will be striving for better corporate governance, more transparency in politics, commerce and the law, and sounder regulation. The cities of Prague, Warsaw and Budapest will have taken their place beside Paris, Vienna and Berlin.

But things could still go wrong here and there. There is the election in Slovakia on September 20th and 21st, which probably won't, but could, put Vladimir Meciar back in office, throwing doubt on Slovakia's membership of NATO and the EU. There is the unresolved dispute between the Czech Republic and Germany over the expulsion of Sudeten Germans from Bohemia in 1945. And there are the shifting Balkans, where ethnic feuds are not necessarily dead and buried.

Existing or incoming governments in Central Europe could reject the conditions for EU entry, which would take the acces-

sion process off course. And even once the new countries are in, EU membership may not prove the panacea they had hoped for. An EU and a eurozone enlarged by perhaps ten members will be even more unwieldy and less sensitive to national priorities. There could be strains that encourage thoughts of a voluntary exit, or the expulsion of an errant government if other sanctions do not work. No one has yet dared write that into a treaty but, with 20-plus members, the time may come.

The biggest change required in the transition countries of Central Europe is in people's attitudes of mind, and that will take time. Silviu Brucan, one of Romania's great survivors—a former adviser to the dictator Nicolae Ceausescu, but no poodle—in 1989 told *Le Figaro*, a French newspaper, that it would take 20 years for Romanians to learn about democracy. "I was sued for offending the dignity of the Romanian nation," he recalls, "but now they say I was an optimist." ■

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Nuclear industry

Fallout

What happens when government uses a privatised company for political ends

BRITAIN'S electricity industry operates under a bracing regime. Energy shall be cheap, reliable, and from diverse, preferably renewable, sources. Generating companies must invest in new technology; neither their profits nor their losses are to be politically embarrassing. Investors interested in this thrilling prospect should please form an orderly queue.

This week's £410m (\$635m) government rescue of British Energy, the country's privatised nuclear power generator, was the inevitable result of the government's ill-formed energy policy. Only three weeks after saying, in mid-August, that it was "not faced with an immediate credit crisis", and despite £615m available for borrowing, managers asked the government for a bailout.

The immediate cause of the crunch was management failure. British Energy's share price plunged after a flurry of bad news about financial and technical hiccups. But even if British Energy's bosses were the best in the business, they would still have suffered from an energy market rigged against them. The government cares chiefly about cheap power, which is popular with voters and businesses. Privatisation and liberalisation in the 1990s made the industry more efficient, revealing a lot of spare capacity—around 25% of peak winter demand. Rejigging the market rules last year pushed down prices further. The current wholesale price is £16 per megawatt hour, about £3 too little for the company to make a profit.

That reflects the complicated legacy of

privatisation and energy policy, which, in recent times, has encouraged the building of cheap gas-fired power stations, while leaving the nuclear industry with heavy extra costs. "This structure could only survive if the electricity price stayed up. But the oil price has trebled; the gas price almost doubled, and the price of electricity has virtually halved," notes Dieter Helm, an Oxford-based energy consultant.

British Energy's burdens are indeed heavy. Whereas competitors that burn gas, oil and coal get off the environmental hook lightly, the nuclear industry must pay £200m annually for its waste to be reprocessed, expensively, at Sellafield, the state-owned nuclear dustbin. That avoids finding a long-term dump to store it in, which would be unpopular, and keeps Sellafield's owner, British Nuclear Fuels Limited (BNFL), afloat. Storing the old fuel, which is what nuclear power industries in most other countries do (see table on next page), would be a great deal cheaper. One of the triggers for the collapse was the failure of British Energy's increasingly desperate attempts to negotiate a much cheaper deal on waste with BNFL.

A second oddity is that British Energy has to pay the government's special tax aimed at reducing CO₂ emissions, even though it emits no carbon. The government justifies this curious imposition by arguing that the tax is designed to encourage renewable energy rather than to penalise the carbon-producers. It costs British Energy £80m annually. There are other handicaps too. Nuclear power stations pay

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Bagehot is unwell

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higher rates (local taxes) than their conventional counterparts. And they also have to provide for huge future decommissioning costs.

The government's short-term loan has now given managers and politicians a couple of weeks to try to sort out the mess. The bravest thing to do would be to let the company go bankrupt. Shareholders and bondholders would suffer, and the assets would go to whoever was willing to pay for them. But that course sounds risky to politicians. Although there is little real likelihood of even a flicker in the electricity supply in the next few years, alarmist headlines—and public worry—would be unwelcome, even if ungrounded.

Arguments are raging about both principles and practicalities. The government, which has promised to publish a new energy policy later this year, is divided. A pro-nuclear lobby, mainly in the energy ministry, wants to prop up or even expand the industry—arguing, for example, that it is the most practical way of cutting greenhouse-gas emissions. The antis think Britain's whole nuclear adventure has been an expensive mistake and that the industry should be run down as quickly and smoothly as possible.

If British Energy is to be kept afloat, the government will have to lighten the politi- ➤



Used nuclear industry, several careless owners

What other countries do

Nuclear energy, 2001

Country	% nuclear	Electricity liberalisation	Waste
France	77	Slow and reluctant	Reprocesses
Japan	34	Just starting	Sends to Britain
Germany	31	EU laggard	Stores
Britain	23	Ahead of most EU	Reprocesses
United States	20	Yes, botched in California	Stores

Sources: www.world-nuclear.org; The Economist

cal burden on the company. It will probably get a better deal on waste and taxes, and plans to release it from its historic liabilities, such as the cost of decommissioning old and clunky nuclear power stations, will probably be speeded up. The government may also give it a management contract—worth perhaps £20m a year—to run Britain's elderly Magnox nuclear power stations, which currently belong to BNFL.

For its part British Energy is hurriedly selling off its overseas assets, in America and Canada, where it is short of the cash needed to satisfy regulators. After that its top managers should start booking lunches with headhunters: the government is peeved by the nasty surprise, and particularly by the company's decision to pay its shareholders a hefty dividend in May, only months before it came begging for taxpayers' money. ■

Politics

The price of war

While Mr Blair worries about Iraq, the unions worry about him

THE prime minister, Tony Blair, says he is willing to pay a "blood price" to prevent Saddam Hussein building up biological and nuclear weapons. But there could be a political price too. Speaking to the Trades Union Congress (TUC) this week, Mr Blair challenged the growing number of vocally anti-war union leaders to forgo rhetoric and work with the government to achieve common goals. "Indulgence or influence—it's a very simple choice," he said.

The prime minister's unqualified backing of American military action against Iraq, however, means awkward choices. Dealing with Saddam and finding extra money for the military is bound to affect domestic politics—starting with a recall of Parliament for a one-day debate in the week of September 23rd, which the government announced this week.

The chief war casualty on the home front could be next year's referendum on the euro. An early date, Mr Blair's initial preference, is expected to slip in the event of war. The longer the delay, and the worse the economic outlook in France and Germany, the stronger will become the arguments for postponing the whole thing. While opinion polls show large majorities against both adopting the euro and attacking Iraq, Mr Blair will not want to risk both an unpopular war and an unpopular referendum.

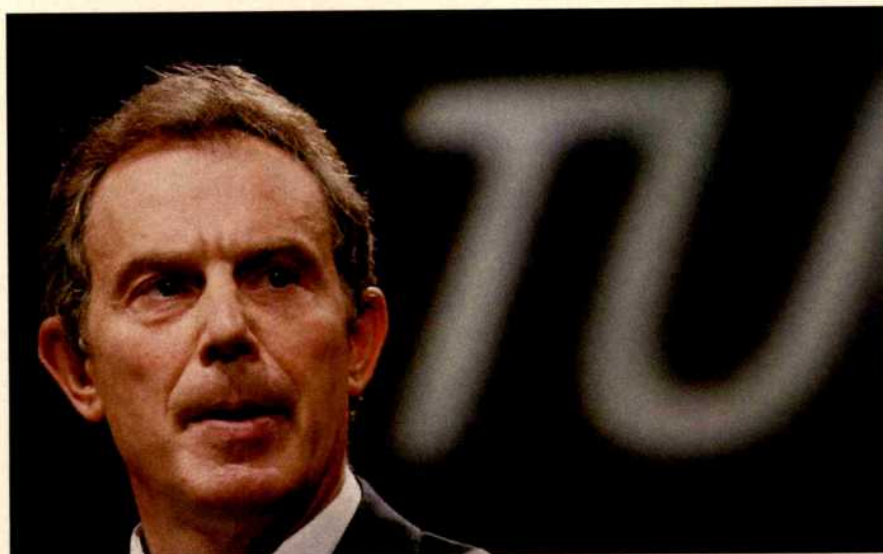
Another possible victim—strongly denied by his allies—is Mr Blair's determination to reform public services. The broad base of union support that sustained Labour's first term of office has eroded. Old friends such as John Monks, the TUC leader, and Sir Ken Jackson, former head of Amicus, the manufacturing union, are leaving the stage. A new breed of noisy left-wing union chiefs has taken power such as Bob Crow (railways) Derek Simp-

son (manufacturing), Dave Prentis (public sector) and Mick Rix (train drivers).

An immediate test of the government's resolve is the threatened national strike by Britain's firefighters, who are demanding a 40% wage increase taking their basic pay to £30,000. The last fire service strike, 25 years ago, went on for nine weeks. The government cannot afford to be seen to cave in but the pay campaign has public support. Both train and tube drivers have promised to help by stopping services. Laws against secondary strikes normally prevent this sort of thing, but the drivers say it would be unsafe to run trains with no firemen available.

All this may be awkward for the government but threats of a return to 1970s-style industrial mayhem are overdone. In truth, the TUC is deeply divided and the union movement has never been weaker. It represents less than 20% of private sector workers; even in the public sector, it has only 59%. For all the militants' hot air, most trade union leaders know that their power is strictly limited and that they have little to gain by sniping from the sidelines. Bob Crow, the fiery leader of the RMT, failed even to be elected to the TUC's governing body this week, the first rail leader not to win election to the general council.

The government will not budge on the unions' more extreme demands for repeal of all the Conservatives' trade union legislation. The employment relations minister, Alan Johnson, a former trade union general secretary, has said there is not "an ice cream's chance in hell" that the government would remove the requirement for ballots before strikes, or allow the return of the closed shop. But Mr Blair cannot ignore union concerns over public-private partnerships, pensions, and employment laws. With the party haemorrhaging members and woefully short of cash, he needs their support more than ever. ■



Fighting talk

Defence companies

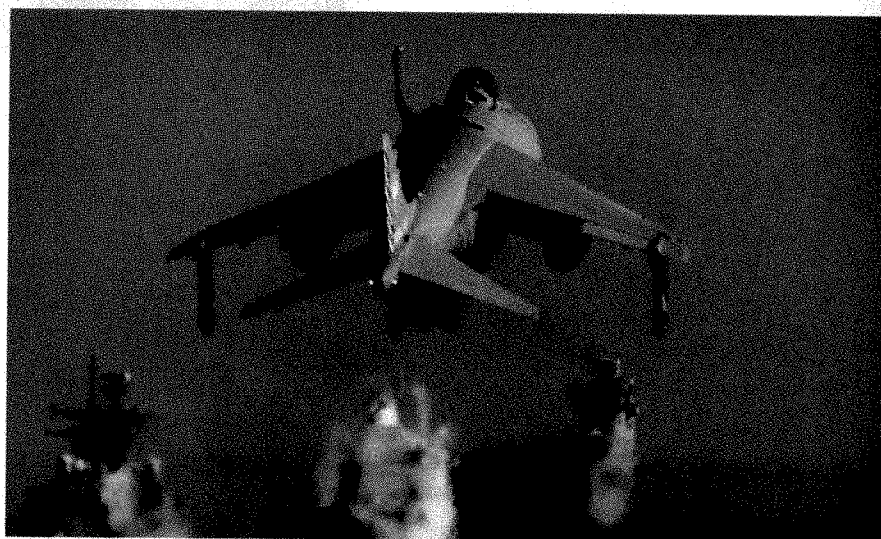
The war dividend

Standing shoulder to shoulder with America is good for business

BITAIN has a large and thriving defence industry, ranking second only to America in the world market. Companies such as BAE Systems (formerly British Aerospace), Rolls-Royce and Smith Group are leading suppliers of defence equipment—mostly related to aerospace, which is by far the biggest part of the defence equipment market.

But this success story may not last much longer. Not that defence is about to decline like coal mines, steel and textiles, whose customers turned to cheaper suppliers in poor countries. Quite the opposite: Britain's defence industry is shifting its centre of gravity to America, where its sales and investments are growing fast. "It's not a trend, it's a bloody stampede," says one industry economist. Sales of defence equipment in America by the top six British defence aerospace companies have doubled since 1997. BAE sells more these days to the Pentagon than it does to Britain's Ministry of Defence.

But this is no rousing story of export success: the sales are largely of equipment made in America by subsidiaries of British firms. "America insists on local production to offset 100% the value of a contract," says Keith Hayward, chief economist at the Society of British Aerospace Companies (SBAC). So even if some widgets are made in the British Midlands or technology is cooked up in Farnborough and sold across the Atlantic, the company will have to make goods of equivalent value in the United States. Most of the manufacturing has to be done in factories that the British companies build or acquire over there.



Heading west

There are clear reasons for this westward migration. First, America is, unsurprisingly, by far the biggest defence market in the world, buying about half of the \$200 billion of military hardware produced in the world each year. And last year's terror attacks have helped trigger a rise in spending on defence equipment, which is tripling from the post-cold war trough it hit in the mid-1990s.

Second, British companies are well received in America because they are seen as trustworthy cousins. The Pentagon worries about sharing technology with the French or Germans for fear it may find its way into the hands of unsavoury regimes. The British tend to comply more easily with American restrictions on export of defence technology. And Britain's readiness to stand by America goes down very well in the Pentagon. Try as they might, continental European defence companies such as Thales and European Aeronautics Defence and Space (EADS) have a harder time getting into the Pentagon. Thales even bought a smallish British company, Racal, partly to use as its ticket to America.

BAE has become very big in America after a string of acquisitions in recent years, taking over parts of American defence contractors that were up for grabs as the local industry reorganised. It also finds it easier than continental Europeans to win Pentagon approval for such deals. Some industry observers even suspect that BAE will one day re-locate its headquarters in America. Its chairman, Sir Richard Evans, explains his expansion in America by pointing out that he has to direct his efforts to the best market.

Defence budgets in Europe are tiny and barely growing. Pan-European projects such as the Eurofighter aircraft take for ever to enter production: the Eurofighter itself is ten years late, and a proposed military transport plane, known as the A400M, has just been delayed again by the Germans

despite being discussed for over 15 years. Military campaigns such as Kosovo and Afghanistan have highlighted the need for more modern transporters.

Outside those cumbersome joint defence programmes, Britain finds it hard to break into the markets of its fellow Europeans. Germany buys little, while France buys only French. Other Europeans with no big home industry tend to buy American because they are cheaper. Britain may be entertaining a bid from a French company, Thales, to build the new aircraft carriers it needs, but it would be pointless BAE trying to do the reverse. ■

Exporting invisibles

PFinancial services

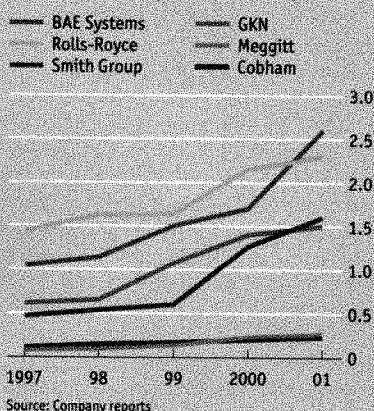
British firms are flogging PFI around the world, and the world is buying

STEPHEN HARRIS is a busy man. He works for International Financial Services, London—formerly known as British Invisibles—which promotes the export of City expertise. Last week he was in Switzerland, this week he's hosting the Estonians, next week it's the Mauritians and the Danes. In fact, Mr Harris is talking to over 30 foreign governments. What is he talking about? The private finance initiative (PFI), which he hopes will be Britain's most eye-catching "invisible" export since privatisation.

"Privatisation", said one of its early champions, "is an ugly word for a beautiful concept." Governments could get shot of underperforming industries, pocket the proceeds and spread popular share-ownership at the same time. Having sold a bunch of Britain's state-owned assets to ▶▶

Land of opportunity

British defence companies' sales in US, £bn





Rejoice, Estonia: the PFI is coming

▶ the public, the City's bankers, lawyers, accountants and consultants went on to sell the idea around the world, as far afield as Brazil and China.

The "private finance initiative" is an ungainly term for a more subtle concept. Rather than selling off assets the government already owns, the PFI raises private finance for infrastructure projects—bridges, hospitals, or prisons—that don't yet exist. According to Tim Stone of KPMG, an accountancy firm, Britain is "ten years ahead of everyone else" in the delicate art of matching private money to public needs. Almost 500 PFI projects have been signed in Britain; nowhere else yet comes close.

But the PFI is not universally loved in its country of origin. The British press and public either ignore it or lampoon it. The unions hate it. In the same week that Mr Harris meets the Estonians, UNISON, Britain's biggest public sector union, is holding a conference accusing the PFI of "Failing Our Future". What do the Estonians see in PFI that UNISON doesn't?

Mr Stone thinks foreign governments are keen to learn from mistakes, as well as successes, in Britain. In particular, the British experience starkly illustrates the importance of getting the contract right. If the contract does not spell out who takes on the risks of a project, they'll usually end up in the government's lap. If the contract does not penalise bad service, then bad service is probably what you'll get. On the other hand, if written well, a PFI contract can align the interests of the financiers backing the project with the interests of the public using the project. If poor service brings poor financial returns, it will be rooted out by ruthless financiers, not tolerated by sleepy bureaucrats.

London buses

Bends v curves

Why mourn creaky old buses when you can welcome new ones

TO LISTEN to the protests, one would think that EuroDisney was taking over the Tower of London. Admittedly, London's dwindling fleet of old-fashioned double-decker red Routemaster buses, like the black taxis and old red telephone boxes, are a distinctive and attractive feature of the city's landscape. It is also true that London's new single-decker bendy buses, which are widely used on the continent (they hinge in the middle and therefore go round corners easily) are foreign, and therefore—to traditionalist tastes—unwholesome and unwelcome.

But reality is more complicated. Passengers will be able to leap on and off the city's 500-odd old-fashioned buses at least until a European directive on accessibility comes into force in (gasp) 2016. London's transport authority says it will consider asking for an exemption even then. By most rational lights, the bendy buses, of which 31 are already in service with another 70 coming by next year, are a welcome innovation. They have a lower floor, making them easier to board. They carry more people than ordinary single-decker buses. They have flat fares, and are cashless. Passengers must buy their tickets in advance, or from a machine, rather than from the driver as in most London buses. These strange ideas work well elsewhere.

But efficiency arguments do not appease the nostalgics. Not only are the Routemaster's curvy lines more beautiful, they argue, but their layout requires a conductor to sell tickets—a social benefit, they claim. Steve Pound, himself once a bus conductor and now a Labour MP, says that this allowed, for example, parents to send their children to school un-

accompanied. "Anything that looks overstaffed can be stripped down by some pinstriped, cocaine-snorting consultant," he complains. "When I worked on the buses, there was a pride, an ethos."

Most bus passengers probably prefer the main features of their bus travel to be cost, safety and reliability, though, which probably means efficiently run new buses, not expensive old ones. Those really wanting the authentic experience can always take the much pricier private tourist buses through London. These invariably use Routemasters, but with the extra benefit of exposure to real British weather on their open-topped upper decks.



Clinging to tradition

Some of Britain's overseas clients have been quite innovative in spelling out what counts as good service. In South Africa, for example, the plan for the Gautrain rail link between Johannesburg and Pretoria includes clauses on black empowerment and local investment. Speaking from Uganda, Charles Morrison of the City law firm Denton Wilde Sapte argues that these new styles of procurement give poorer African governments, in Uganda, Ghana or Tanzania, the chance to decide for themselves what their needs are and how they should be met, rather than having their donors decide for them.

For some overseas governments, PFI may have another, less noble, appeal. Mr

Harris admits that some of his guests roll up thinking PFI is a way to get "free infrastructure". It's certainly not that. As he and Mr Stone emphasise, the government pays for the services the infrastructure provides, and these payments, extending over 20 or 30 years, must be generous enough to attract private finance in the first place. Since private finance is usually more expensive than public finance, PFI's critics see it as a costly way for governments to shift borrowing off their books. If overseas governments do see PFI as a neat accounting trick, it will no doubt be a hit export, improving Britain's invisible overseas trade. Whether it will visibly improve overseas infrastructure is another matter. ■



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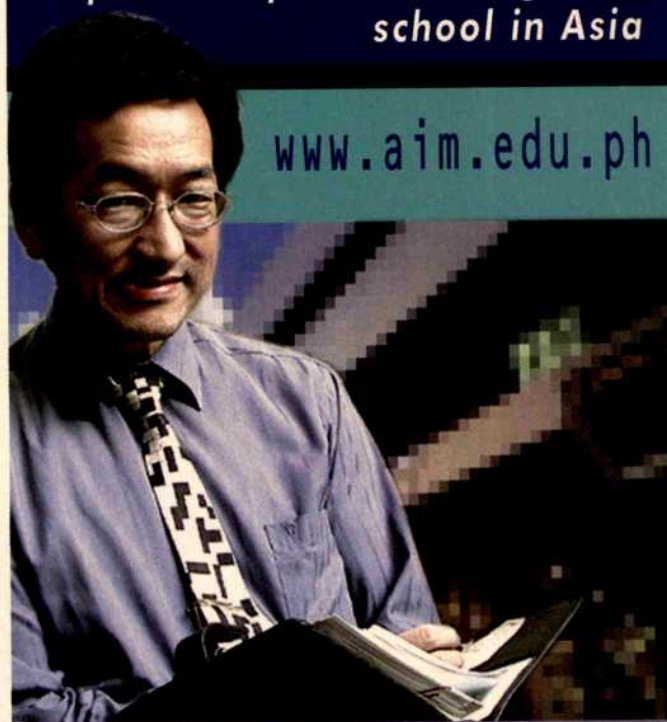
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White-collar crime in America

Out to catch the big fish

NEW YORK

How goes the war against corporate crooks?

AMONG the underpaid and overworked lawyers who make their careers in public prosecution, there is one job that can make a lifetime of slog worthwhile: US Attorney for the Southern District of New York. So when James Comey told his wife that the White House had telephoned to offer to uproot them and their five children from Virginia to Manhattan, she burst into tears. "You can't say no," she told her husband. "I didn't," he replied.

Mr Comey was previously appointed to work in the attorney's office when Rudolph Giuliani, celebrated former mayor of New York, was its boss. Then it was running a collection of headline-grabbing insider-trading cases that helped to refine Wall Street. Nine years later, Mr Comey finds his old office at another historic juncture. The bursting of the stockmarket bubble of the late 1990s has exposed abundant evidence of accounting fraud. A new and broader-based investing public has lost an awful lot of money. The perpetrators appear to have pocketed tens of millions of dollars. Confidence in the fairness of America's capitalist system is said to be at risk. Heads have to roll.

Mr Comey's office is not running every current big corporate-fraud case. Because of potential conflicts of interest among prosecutors in Houston, the bulging file on Enron has been given to a national team of prosecutors run by the Justice Department in Washington, D.C. Certain tax aspects of

the case against executives at Adelphia belong to the US attorney's office in Pennsylvania, where the company has its headquarters. But Mr Comey's office has claimed the lion's share of the work.

Its 230 prosecutors are responsible for WorldCom, which allegedly disguised deteriorating results through massive accounting fraud; the important bits of Adelphia, a publicly owned firm whose founding family helped itself to riches; and ImClone, a biotechnology start-up run by a Manhattan socialite whose alleged insider trading ensnared Martha Stewart, America's doyenne of soft furnishings (see page 59). More cases may follow, including Sunbeam, a bankrupt home-appliance company whose former boss, Al "Chainsaw" Dunlap, has been accused of cooking the books.

That these cases are only just beginning to show public signs of progress (see box on next page) has been a source both of anxiety for Justice Department officials and of political pressure on the prosecutors. With outrage following outrage in the media, politicians have been clamouring for quick public hangings. Tom Daschle, the Senate majority leader, put his finger on it in June, when fresh evidence surfaced about WorldCom's misdeeds. "Somebody needs to go to jail," he wailed.

The Justice Department seems to agree that there may be a problem of slow speed. One of the ideas that its corporate-fraud

task-force, a sort of legal think-tank set up to absorb political pressure, has been floating is to bring more less-than-airtight cases before juries, as an antidote to the conservative instincts that white-collar crime encourages among prosecutors.

Prosecutors have some things going for them. The advent of e-mail is one. Most companies keep complete e-mail archives, and if they don't, the library can usually be rebuilt. "Flipping" underlings—accepting their co-operation, plus a guilty plea, to get at the top ranks—is another tactic. Last month, Michael Kopper, who worked in Enron's finance department, pleaded guilty to money laundering and conspiracy to commit wire fraud. The account of his crimes that he gave suggests that the bigger target is Andrew Fastow, Mr Kopper's boss and Enron's former chief financial officer. As the defendants become more important, however, this tactic loses its force: Mussolini gets a deal, as it were, only if he can deliver Hitler. Defendants also have less incentive to co-operate following the introduction of less flexible federal sentencing guidelines in the 1990s.

Subpoenas of witnesses by Congress can hurt the prosecution's case, especially if they give others information about how to build a good defence. Most Enron executives "took the fifth" (the fifth amendment to America's constitution, which protects citizens from self-incrimination) and declined to testify before Congress. But Jeffrey Skilling, a former chief executive, did testify, maintaining his innocence and his faith in the sound judgment of the firm's lawyers and accountants. Others now know Mr Skilling's defence, and can co-ordinate theirs accordingly. Significantly, Congress chose not to subpoena Martha Stewart this week.

Defendants have the best lawyers that a multimillion dollar executive-com- ➤

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pensation plan can buy, and several good strategies available. One is to seize the prosecution's ground and to acknowledge the crime, but not the criminal. Their client, goes this line of defence, simply did not know that he or she was doing something wrong. Ms Stewart might have a hard time making this defence: she was once a broker. But Scott Sullivan, WorldCom's former chief financial officer, could make a case along these lines, as he appears to have made no effort to cover up his misclassification of expenses. The surprise is how naked and obvious it all looks.

Mr Comey's young guns are not experienced. Only one in ten of his prosecutors has spent more than five years in his office. Typically, they work like dogs for a few years, then move on to the comforts of private practice. Complicating matters, prosecuting white-collar crime can be a high-profile business, played out in the full glare of television cameras.

The recent dawn arrest of John Rigas, Adelphia's founder, along with two of his sons, raised all sorts of briefly compelling side-issues. Was it a publicity stunt orchestrated to slake the public's thirst for blood? (Answer: No. The arresting officers rang to ask how they should handle the business; Mr Comey told them to treat the Rigases as they would treat anybody else.)

The disarmingly modest Mr Comey appears unruffled by it all. He doesn't seem to care what politicians want or don't want; he doesn't seem to care much about the markets either. What he does care about "is that the bad guys go to jail". ■

Indictments

The charge sheet

NEW YORK

So far, so few

THE wheels of justice turn mighty slow. But they turn. Here is a list of the indictments so far:

- In March, **Arthur Andersen** was indicted by a federal grand jury on charges of obstructing justice.
- In August, **Michael Kopper**, a senior executive in **Enron's** finance department, pleaded guilty to money laundering and conspiracy to commit wire fraud.
- **Scott Sullivan**, a former chief financial officer of **WorldCom**, was indicted in a Manhattan federal court along with **Burford Yates**, WorldCom's director of general accounting. Mr Sullivan and Mr Yates are each charged with one count of conspiracy to commit securities fraud, one count of securities fraud, and five counts of making false filings with the SEC. Mr Sullivan and the company's former comptroller, **David Myers**, were arrested on August 1st on securities-fraud

Japanese car makers in America

Twenty years down the road

TOKYO AND DETROIT

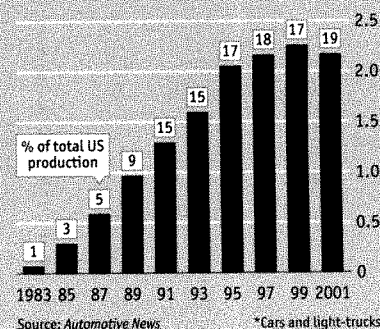
Toyota may be about to join the ranks of America's Big Three car makers

TWENTY years ago, the finishing touches were being added to the first Honda cars to roll off the production line at the first Japanese car plant in North America, in Marysville, Ohio. The Japanese manufacturer was there in response to taunts by a Ford chairman, Harold "Red" Poling, that the Japanese should "build cars where they sell them". In the protectionist mood of the times, the only way Japan's car companies could get round import restrictions was to invest directly in America. Honda, which already had motorcycle production there, was the first, followed over the next four years by Nissan and then Toyota.

So successful have their cars been since then that Toyota is now poised to replace Chrysler as number three in the American car market, with over two-thirds of its sales manufactured locally. Until American manufacturers rolled out interest-free finance schemes in desperation in September 2001, Toyota had looked like overtaking Chrysler, the weakest of Detroit's Big Three. Yet, only two years earlier, Chrysler's market share had been almost 1.5 times that of Toyota.

Driven by boomers

Japanese vehicle* production in the US, m



"Toyota's market share goes up during downturns," says Yukitoshi Funo, head of the company's North American operations. Sure enough, its American car sales in the first eight months of this year rose by 4.6% over the same period in 2001, in contrast to declines at Ford and Chrysler. This rate made Toyota's president, Fujio Cho, speculate in New York last week that the company may soon "be in need of another plant" in North America, its fifth, to meet its sales target there of 2m units by 2004.

All three top Japanese manufacturers have ambitious plans to increase their global sales over the next few years, and they see America as the most promising place to grow. It is also where they make well over half their profits, their home market being flat and their European plants still loss-making. Whereas General Motors (GM) makes only about \$330 in profit per car, Toyota and Nissan make around \$1,000, and Honda over \$1,600.

Before the Japanese set up in America, people like Mr Poling thought the secret of their efficient car-making was superhuman labourers working like crazy on the assembly lines back home. So it was a big surprise to complacent American manufacturers when Honda started making cars equally efficiently, using American workers on American soil. Of course, the Japanese were careful to steer well clear of the Detroit area, so avoiding the clutches of the United Auto Workers (UAW) union and its then resistance to modern manufacturing methods. The most efficient car factory in the world is Nissan's plant in Smyrna, Tennessee, where the UAW lost heavily in a recent vote to represent workers.

American consumers soon learned that the real secret of Japanese success was ►►

▶ that the manufacturers concentrated on such basics as product quality, inventory control and market research. This is still working to their advantage. Durability and economy matter when times are hard (and fuel prices are rising), since penny-pinching consumers look for cars that wear well and are frugal. Improved servicing facilities have also boosted sales. A reputation for reliability brings other benefits. Second-hand Toyota Corollas and Honda Accords sell at higher prices than comparable cars made in Detroit. One study showed that GM-marqued cars rolling off its joint plant with Toyota in California were worth less after a few years than identical cars with Toyota badges.

Toyota and Honda have maintained their advantage in other ways. Unlike their American rivals, they have set tight limits on fleet sales to car-rental companies; consequently, their used-car markets are not flooded with car-hire cast-offs. They have also avoided the huge financial incentives that most American car companies now shower on their customers.

Toyota has worked hard at staying close to its dealers. High-level executives visiting from Japan often make a point of calling on dealerships to chat with salesmen. When car sales began falling in 2000, Toyota soon heard from unhappy salesmen that stocks of unsold cars were starting to build up, and it hastily reduced production. American car companies were slower to respond.

Steve Usher, a car-industry analyst at J.P. Morgan in Tokyo, says that another reason why Toyota and Honda have done well is that they have grown up with America's baby-boomers. Japanese cars entered the market in the 1960s and 1970s,

when Detroit was still concentrating on building powerful engines rather than raising overall quality. As new entrants, they offered smaller, cheaper, more fuel-efficient vehicles that appealed to the (then) young. As that generation grew older and richer, the Japanese car makers followed them by moving into the luxury end of the market, with brands such as Lexus and Infiniti.

Now that they make light trucks, such as pick-ups and sport-utility vehicles, in America as well, the Japanese have increased to 20% their share of that part of the market (Detroit's last redoubt through the 1990s). Mr Usher thinks they may soon match their one-third share of the saloon-car market.

But the Japanese cannot afford to be complacent. The Indiana factory shared between two smaller Japanese car makers, Isuzu and Subaru, has stopped production because of weak sales. Even Toyota has made mistakes. The T100, initially a big flop, took off only after the company completely overhauled the truck and relaunched it as the popular Tundra; but it is once again under pressure from rivals. European companies are also increasing their North American production: Mercedes is expanding in Alabama, and Volkswagen is considering adding a United States plant to its facilities in Mexico because sales have rocketed since the new Beetle was launched five years ago.

All this means that the Japanese have little room to make mistakes. Being bigger, Toyota can afford to run more risks than Honda. But it is vulnerable to the fact that, although its cars delight and its factories astound, its management remains distinctly old-fashioned and Japanese. ■

French bosses

Bon voyage?

Imitating American ways is no longer the fashion in corporate France

THIS WEEK, as *The Economist* went to press, the final touches were being put to a rescue package for France Telecom, labouring under debts of €75 billion (\$73 billion), six times its market capitalisation. The rescue was due to be announced, with another set of awful results, on September 13th. The most likely solution: a rights issue to raise as much as €15 billion, of which half will come from the government, as 55% owner. Michel Bon, who as the company's boss is most responsible for its travails, is unlikely to keep his job.

Dashing, Anglo-Saxon-style bosses such as Mr Bon have been out of favour in France ever since the decline of Vivendi Universal. Solid, older types with unblemished records are now in; red (ink) has put grey back into fashion. The man who succeeded the flamboyant Jean-Marie Messier as head of Vivendi was Jean-René Fourtou, a former boss of Rhone-Poulenc who is the ultimate in low-key sobriety.

The new conservatism is understandable. It is not only the more adventurous outriders of French business who have come to grief. The two most famous home-grown corporate empires, the retail group of François Pinault and the luxury-goods firm of Bernard Arnault, are struggling with a series of reverses. Even Serge Tchuruk and Pierre Bilger, bosses of the once-solid manufacturing firms Alcatel and Alstom, respectively, are in difficulty.

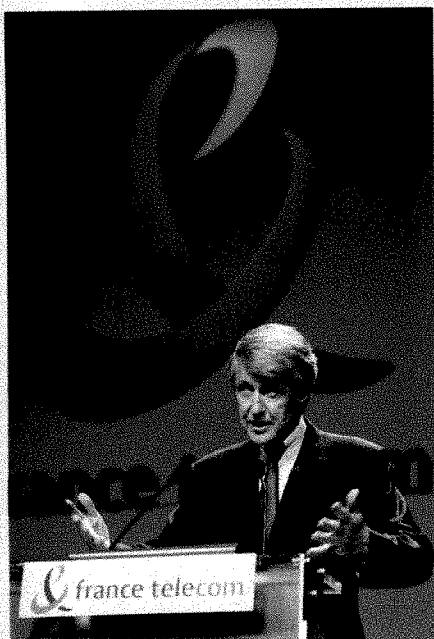
In such circumstances it is no wonder that the two favourites to follow Mr Bon at France Telecom are proven local leaders, well-connected to political power. Thierry Breton, chief executive of Thomson Multimedia (the consumer-electronics part of the formerly state-owned Thomson-CSF group), was a local politician in the west of France who made his business reputation running the Futurscope leisure group; he is close to the prime minister, Jean-Pierre Raffarin. Noël Forgeard, chief executive of Airbus, has been a close friend of President Jacques Chirac since his days as industrial adviser to the then prime minister in the second half of the 1980s.

The France Telecom job might be a challenge even for Mr Forgeard, but it would get him out of an awkward spot. He has had a highly successful three years at Airbus, converting it from a consortium into a commercial company, launching its double-decker super-jumbo, and catching up with its rival, Boeing. But he is frustrated.

Airbus is 80% owned by European ▶▶



The first of millions



In the Bon old days

► Aeronautics Defence and Space (EADS), and 20% by BAE Systems. Although jet airliners account for two-thirds of EADS sales and almost all its profits, Mr Forgeard has to report to EADS's bosses. Although he has never said so publicly, it is plain that he would like to take over from the French co-chief executive, Philippe Camus.

One German analyst likens the situation to that of Daimler-Benz when the aggressive Jürgen Schrempp took over in the mid-1990s. The group's luxury-car division, Mercedes-Benz, under the direction of Helmut Werner, was making virtually all its profits at the time. But Mr Schrempp decided the group was not big enough for two abnormal egos. So out went Mr Werner, the architect of the Mercedes revival in the early 1990s.

Airbus's problems are bigger than a mere clash of egos. The old guard at Aerospatiale, the engineers and managers who built Concorde and launched Airbus, were put out when the French government first privatised the group by selling a big chunk of it to a conglomerate created by Jean-Luc Lagardère, a controversial wheeler-dealer who has outstayed the more recent shooting stars.

Respected for his cool efficiency in reforming Airbus, Mr Forgeard is nevertheless snootily referred to in Toulouse as "one of the Lagardère boys". Nor has he done much to ingratiate himself with his German bosses: he made Philippe Delmas, who is seen as anti-German because of a book he wrote about world affairs a few years ago, his strategy director. Having done what he was hired to do at Airbus, and frustrated in his bid to rule EADS, no wonder Mr Forgeard's name keeps cropping up as a candidate for top jobs among France's beleaguered businesses. ■

KarstadtQuelle

Below par

HAMBURG

The boss of the big German retailer is pinning his hopes on golf

SOME say golf is a good walk ruined. Not Wolfgang Urban. The chief executive of KarstadtQuelle, a big German retailer, thinks more Germans will be seduced by the game—and will buy their gear from KarstadtQuelle. It is one of the ways in which he hopes to improve the company's currently miserable margins.

Retailing in Europe's biggest economy, with 82m mostly well-off people, may sound a doddle. It is not. Margins are thin, thanks to fierce price competition, a surfeit of selling-space and weak demand. Retail sales have scarcely budged since the fading of a post-unification surge in the mid-1990s (see chart), and they have fallen every month this year. According to one of Mr Urban's rivals, business has rarely been as bad since the second world war.

At Karstadt, the biggest department-store chain in Europe, sales in the first half of this year were 9.5% lower than in 2001. KarstadtQuelle, its parent, lost €347m (\$311m) in the first six months of the year, and its share price has fallen by 50% since the spring. To some extent, these troubles are temporary. Shoppers suspect retailers of using the introduction of the euro in January to mask price increases. Like Karstadt, Thomas Cook, a travel company of which KarstadtQuelle owns half, is in a suffering seasonal business.

KarstadtQuelle has, however, been struggling for more than a few months. Its exposure to Germany, where it makes 90% of its sales, has scarcely helped. Its bigger rival, Metro, where Mr Urban worked for 25 years, also has a troubled German department-store chain, Kaufhof, but it has been partly redeemed by its substantial cash-and-carry business, which operates in 23 countries.

Since becoming chief executive two years ago, Mr Urban has been firing off bright ideas for making money. The plan is to raise margins to 4% by next year: good by German standards, but only half the European norm. The firm is only now exploiting the stack of information—from customers' addresses to their taste in clothes—held by its department stores and two mail-order subsidiaries. The result—store cards, Karstadt-branded credit cards and direct marketing—may be old hat in America or Britain, but in Germany they are still near-novelties.

KarstadtQuelle has also been cutting costs, becoming stingier with its suppliers and shedding 7,000 jobs this year. Yet de-

spite Germany's glut of retail space, it is still reluctant to close any shops. It has 189 department stores, the same as a year ago. Quite a few are in small towns and suburbs, and it owns almost all of them. Indeed, the value of its property portfolio exceeds its market capitalisation, suggesting that the shops could be put to better use. Karstadt is due to reveal plans for its smaller stores in November.

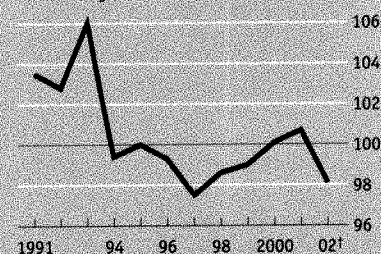
Some could become specialist shops rather than department stores. There is money to be made, Mr Urban believes, from more specialisation. Sport is a prime example. By 2005 KarstadtQuelle, already the market leader, expects to sell €1.2 billion-worth of equipment and clothing, up from €650m last year. The number of big, general sports shops, such as its flagship 6,000 square-metre store in central Hamburg, will rise to 35, from around 30 now. There will also be more shops with a narrower focus, including a total of 31 devoted to Mr Urban's beloved golf, hitherto an exclusive sport in Germany.

Eventually, KarstadtQuelle might open sports shops abroad. That would reduce its dependence on Germany. Home, though, is the key. The company expects not only to win a bigger share of the German sports-goods market—largely by taking over uncompetitive small firms—but also to fatten its margins, 2.3% last year, to 6% in 2005. However, cheaper competitors, including supermarkets and Tchibo, a coffee seller that also flogs cheap but presentable clothing and household goods, have their eye on the market too. Mr Urban's hope is that quality will count as much as price: in his shops, people will get advice that discounters cannot offer; and he reckons Karstadt's own label, Alex, will command a premium that cheaper rivals will not.

Juicy profits may be on offer in some plush niches, such as golf, assuming the market grows as Mr Urban hopes. In other areas—sports clothing worn as fashion, say—the German market may prove as tough as it has always been. Mr Urban will need luck as well as his experience and skill. It's a bit like golf, really: even well-hit balls can end up in the rough. ■

Shoporexics

German retail sales volume*
annual average, 1995=100



*Excludes car dealers and petrol stations
†Average of first seven months, seasonally adjusted
Source: Federal Statistics Office

Enel

An ill Wind

ROME

Enel's new boss is taking the utility back to its roots

DELIVERING Enel's otherwise routine half-year results on September 12th, Paolo Scaroni, recently appointed chief executive of Europe's biggest listed utility, gave the markets a shock. In his characteristically open style, he announced an entirely new strategy for the diversified group. The man who turned around Pilkington, a troubled British glass maker, made clear that he is junking the grandiose ambitions bequeathed by Franco Tato, his predecessor, and returning to the core energy business: power generation and the distribution of electricity and gas.

Under Mr Tato, Enel had aggressively diversified into activities ranging from water to telecoms and even payroll-processing. By announcing such a sharp break with the recent past, Mr Scaroni has begun the job of restoring confidence in a company that was Italy's biggest privatisation. Since its flotation in November 1999, Enel's shares have fallen heavily. Such a poor performance has disappointed its shareholders, and Enel's tetchiness has annoyed regulators, government ministers and investors alike.

Mr Scaroni inherited a vastly complex structure, with more than 30 managers reporting directly to him. Now there are only four. But the most awkward part of Mr Tato's troubled legacy is Wind, Enel's telecoms arm (of which France Telecom owns 27%). Although well ensconced as Italy's third-biggest mobile operator, Wind is making losses and is heavily in debt. On September 12th, Mr Scaroni said he was writing €1.5 billion (\$1.46 billion) off Wind's book value of €9.5 billion. Enel will have to pump €1 billion of cash into the business before it can become financially independent, a benchmark that is at least two years away.

The clear implication is that Wind will be nurtured through the telecoms downturn until it can be sold for a reasonable price. "There are few synergies between telecoms and energy, and these are not allowed by the regulator," says Mr Scaroni. Add in his stated intention to get out of the water business and a host of other non-core activities, and Enel is destined to re-emerge as a more efficient version of the energy company that it was back in the mid-1990s.

Investors are likely to welcome this refocused focus. Mr Scaroni says that his first priority is to instil a culture of shareholder value within the company. Without this,

Enel will not attract the big international investors whose support is vital to such a large concern. Hence, for example, its new approach to expanding outside Italy. Mr Scaroni says future deals will be opportunistic and must make immediate financial sense. Logical acquisitions in markets such as Spain, Eastern Europe and neighbouring countries, with which cross-border electricity trade will be possible, will replace the far-flung ventures that were pursued by Mr Tato.

A further important step will be a renewed focus on Enel's domestic energy market. By becoming the low-cost producer and distributor while the market is opening up, Mr Scaroni thinks Enel can hold new entrants at bay. This is also the key to producing the hefty cashflow that will be needed to underpin a generous dividend policy—more than half of Enel's 2001 earnings were paid out to shareholders, not least among them the Italian government, which still has a 68% stake.

A big issue facing Mr Scaroni is whether the government will allow him to run the company as he sees fit. "So far," he says, "there has not been much difference at all in corporate governance from what I was

used to at Pilkington." That could change, however. Last month the government arbitrarily suspended a tariff rise, at a cost of €40m to Enel. Worse, legislation is in hand that would effectively emasculate Italy's independent energy regulator. By handing control of supposedly liberalising markets back to the politicians, it would run entirely contrary to EU policy.

In the short term, however, such shenanigans could help Enel. By a twisted logic, the more the state interferes, the less foreign investors will be attracted to the Italian market and the less competition Enel will face. The longer-term effects, however, are likely to be invidious. Enel's future competitiveness depends on its ability to become more efficient. For that, Mr Scaroni needs a free hand both for internal restructuring and external negotiations, especially with regulators.

Mr Scaroni says he will leave the company rather than tolerate state meddling. That would have a disastrous effect on Enel's share price and, by ruling out further privatisations, on Italy's public finances. Mr Scaroni might appear vulnerable, but he has some cards. Enel's fortunes stand or fall on how he plays them. ■

Endemol

The reality after the show

HILVERSUM

How long should the granddad of reality TV stick to the genre?

A YEAR ago, reality television was being dismissed as a short-lived fad. "Big Brother" (a European hit) had disappointed in America; "Survivor" (an American hit) had flopped in Britain. A year on, and the world's small screens this autumn are once again crammed with reality shows. Last week's final of "American Idol", a talent contest, drew a massive 23m viewers. In Britain this summer, "Big Brother 3" beat each of the previous series.

Yet Endemol, the Dutch-based production company that devised and produces "Big Brother", "Fear Factor" and a host of other formats, is now wondering how to diversify its wares. No company embodies reality TV more than Endemol. Its rise has been as swift as has the tendency of high-minded critics to pan its output. Just eight years ago, two Dutch TV producers, John de Mol and Joop van den Ende, merged their businesses to create their eponymous Dutch company. Since then, it has hoovered up or launched production companies in 22 countries, to become the producer of almost every format it creates. And on top of all this, its founders sold out at the height of the media boom in 2000 to

Telefonica, a Spanish telecoms group, for a staggering €5 billion (\$4.8 billion).

Creating over 15,000 hours of programming last year, Endemol is now the most prolific pan-European TV producer. And it has continued to grow through the media downturn. In 2001, its revenues jumped by 63% over the previous year—to €914m. ▶



A close shave, courtesy of Fear Factor

By contrast, over the same period, revenues at FremantleMedia, its nearest rival, which is owned by Bertelsmann's RTL and is behind the format of "American Idol", grew by just 5%.

Endemol now faces three big strategic questions. The first is whether, as a supplier of content, it also needs a distribution channel. The second is how it can protect its entrepreneurial creative spirit inside a big, unwieldy organisation. And the third is whether it should continue to concentrate on the one-off "event tv" business, in which a show may storm the ratings one summer but then disappear.

In theory, Endemol already has a distribution outlet through its parent company. But Telefonica's tv interests are mainly in Spanish-speaking countries, and its biggest business is telecoms. Synergies between it and Endemol have been minimal. At a time when media conglomerates are going out of fashion, it might seem odd to suggest, as some observers do, that Endemol should free itself from Telefonica and become part of one. Mr de Mol insists that "good product always finds its way to the consumer", and that he is not actively seeking a broadcast channel. Yet Endemol is keenly aware that, with no favourable treatment from a broadcaster, it is heavily dependent on its hits and its ability to keep creating them.

The very idea of belonging to a traditional media giant would, however, exacerbate the second problem the company is grappling with: the need to balance its Dutch headquarters' desire to keep control with its local operations' wish for creative freedom unburdened by bureaucracy. So far, the company has resolved this conflict by allowing each country to get on with devising ideas for its local market, while the chain-smoking Mr de Mol runs his own creative unit in the Netherlands.

Made up of some 20 people, this team concentrates on ideas for the international market, for both tv and other media. The creative heads meet frequently, as do the business heads of each country, to swap ideas. This flexible structure, along with the company's relatively cosy size—it has only 3,300 employees—makes it fleet-footed in getting ideas from paper on to the small screen.

So far, the formula has succeeded. Endemol's library holds some 500 formats, of which 300 are being produced at any one time. The company has a creative buzz about it that lures young producers. Yet the qualities that drive Mr de Mol's creativity are not equally suited to the daily grind of improving operating performance and sitting in committee meetings. One of the oddities about Endemol is that it has no chief executive as such. But Mr de Mol is its chairman and chief creative officer, and also, in effect, the boss.

For now, Endemol's unorthodox man-

agement structure seems to be working. Yet depending on one-off hits is risky; and making them last is difficult. Which cuts to the third of the big strategic issues facing the company.

Certainly, the temptation is for Endemol to stick with reality tv. It is cheap to make: there are no stars to pay. And it can generate extra revenues from telephone calls, interactive voting and text-messaging—not to mention the records, books and spin-off merchandising. As Tom Barnicoat, chief executive of Endemol UK, says, "off-screen revenues are increasingly critical to the business model for a tv programme." The formula has also so far proved to be more enduring than many imagined.

Yet the company is keen to balance its reality-tv output with programming that brings in steady revenues, week in, week

out. Its Dutch operation already produces lots of soaps and other cheap forms of popular drama, such as police and hospital series, which have more lasting franchises. As they grow, the overseas businesses are looking to do the same.

For now, however, reality tv is serving Endemol well. The company seems to have an inexhaustible supply of variations on a theme, ranging from the merely voyeuristic to the grotesque. The world can thank it for "Big Diet", a format in which ten fat candidates move into a house and race to get thin. Or "Exhausted", devised by its American arm, in which contestants are deprived of sleep and then made to perform tasks. Mr de Mol is unapologetic. "The only criticism I agree with is that they are voyeuristic; but that's just normal human behaviour." ■

Luxury submarines

One-downmanship

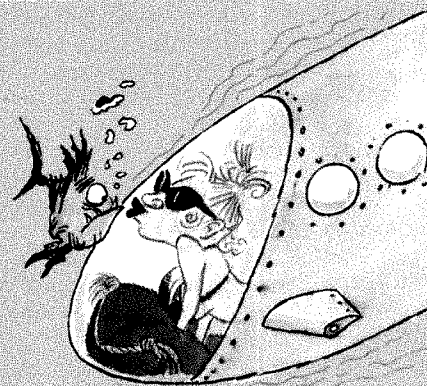
WASHINGTON, DC

Now you really can live in a yellow submarine

LANCE BASS, boy singer with the group L'N Sync, must be feeling down. His bid to fly to the International Space Station fell through when he was unable to raise enough cash for the return fare. But he might raise his spirits by lowering his sights. For half the price of going up he could go down, to a world nearly as unexplored as space. He could buy a personal luxury submarine from one of two American companies, Olympic Submarine Technologies and US Submarines, now marketing it as the latest "ultimate accessory". Microsoft's co-founder, Paul Allen, is said to be among the first buyers.

On offer in a range of sizes, diesel-electric luxury submarines can be fitted out like top-of-the-range business jets and hoisted on and off your personal cruise-ship. Or, indeed, they could be a personal cruise-ship, just like the ocean-going bimbo carrier belonging to your neighbour in the harbour except that it can also cruise below the waves. How about that for one-downmanship?

"We're bringing super-yacht interior amenities together with technologies from military, commercial and tourist submarines to produce true luxury vessels," says Jim Carnahan, Olympic Submarine Technologies' director of marketing. Olympic is offering the Olympic 40, a 40-footer capable of cruising at a depth of 1,200 feet for eight hours. The interior includes an elegant passenger compartment, bathrooms, a galley and large windows through which to view the wonders of the deep. Mr Carnahan believes that the "surface



is just being scratched" in terms of the technology they could incorporate.

L. Bruce Jones, co-founder of US Submarines, agrees. His company plans a range of luxury models—from 65-foot diesel-electric ones with passenger space similar to a medium-sized executive jet, for \$4.5m, to 118-foot varieties with five state rooms and a transatlantic range, for just \$20m. Both firms stress the advantages of submarines: a superior ride in rough seas (below the surface), and a consistent atmosphere. "Regardless of depth you're in shirt-sleeved, air-conditioned comfort," notes Mr Jones.

Both firms are going after the same group of customers—people attracted to luxury yachts. Mr Jones believes the potential market could be as big as \$100m a year. "Most people haven't viewed any portion of the sea floor. Cruising along the continental shelf there's no telling what you might encounter." Not, it seems, rock-bottom prices.

Face Value Cooking Martha's goose

The Martha Stewart scandal may cripple a media empire built on an image of perfection



THE heat is turned up, and the ingredients are blending into America's juiciest financial scandal. In the pot is Martha Stewart, the homemaking queen who has baked, decorated and, say critics, clawed her way to star status and huge personal wealth. Ms Stewart, 61, now faces the double jeopardy of a possible jail term and of being ousted as boss of her closely controlled media empire, Martha Stewart Living Omnimedia.

She is under investigation for possible insider dealing, when she sold her shares in ImClone Systems the day before the biotech company announced that its main drug had failed to satisfy the regulators. Perhaps equally serious, she is also being investigated for obstructing justice by lying to prosecutors about the details of her share sale.

Although she has so far escaped being charged, on September 10th her case was passed to the Justice Department at the urging of a congressional committee before which she had refused to testify. ImClone's former boss, Sam Waksal, Ms Stewart's friend and her daughter's ex-boyfriend, has already been arrested on charges of insider dealing. Omnimedia, worth \$2 billion at its peak, has seen its share price fall by 60% since the scandal first emerged in June (see chart). Last week, the company was forced into an official denial that it was seeking to replace Ms Stewart, its chairman, chief executive and controlling shareholder.

Pressed pansies

Martha Stewart's image is, in short, in tatters. Jokes about how to sponge-paint a cell wall abound. The media lambasted a priceless moment on her weekly CBS breakfast spot, now on hold, when, asked about the scandal, she chopped savagely into a cabbage, grating: "I want to focus on my salad". Meanwhile a bestselling biography published this spring paints her as a "Queen of Mean" control freak.

If the allegation that Ms Stewart illegally avoided a potential loss of \$270,000 sounds trivial next to the breathtaking frauds at Enron and WorldCom, this underestimates the enduring fascination that she holds for Americans. Martha Kostyra, a Polish-American from New Jersey, spent her teens sewing her own dresses and cooking for a family whose poverty and abusiveness she later tried to hide. Following a stint as a model, she became a stockbroker at a firm that, prophetically, tanked after a share-dealing scam.

It was the act of restoring a wrecked house in Connecticut with her ex-husband Andy that steered Ms Stewart, a workaholic fuelled by ambition and chronic insomnia, towards homemaking as a career. Her gourmet-food shop became a catering business and in 1982 she published her first book, the best-selling "Entertaining". Her business instincts, even then, were formidable. In 1987, she persuaded Kmart to sell and market her products, at a huge cost to the now-bankrupt nationwide retailer.

The effect was to turn her into a household name. She talked Time Warner into funding "Martha Stewart Living" magazine, which became a hugely successful title. When Time Warner dismissed her plan to cross-sell her publishing, TV, merchandising and Web interests, she bought back her brand rights and, in 1999, took the entity public just as sales were soaring. Turnover hit \$296m in 2001.

Half of America is in awe of her success and determination. But the other half delights in debunking her carefully constructed mythology, pointing to the tortured personality that lies behind it. Stories abound of how she has exploited friends, belittled her ex-husband and once tried to back over a gardener in her pick-up truck. One store in California is trading equally well in "Save Martha" T-shirts and in ones with her smiling face behind bars.

That is what makes the ImClone allegations so dangerous to the Martha Stewart brand. While Ms Stewart's public image has always had an edge—more dominatrix of domesticity than goddess of goodness—its essence is her perfection. Capitalising on the chronic insecurity of Americans in matters of taste, she branded herself the ultimate authority on perfect living, be it making coasters from pressed pansies or whipping up dinner for 20 in half an hour. Now her image is

looking a sham and Ms Stewart appears just as fallible, greedy and, above all, naive, as her public. For a government seeking a symbol of corporate greed, Ms Stewart, a well-known contributor to the Democrats, is, well, perfect.

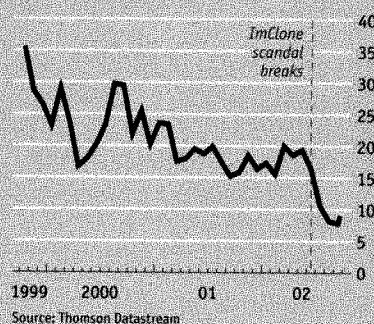
The sullied reputation of its founder is sure to have serious consequences for Omnimedia. Already the company has given warning that third-quarter profits will be half Wall Street's forecasts and that advertisers are taking a "wait-and-see" attitude to future bookings. The company's president, Sharon Patrick, plans to promote "new faces" to take the spotlight off Ms Stewart. But as the embodiment of an abstract marketing message, Martha is surely irreplaceable. Without free advertising from her ubiquitous TV shows, a syndicated column in 230 newspapers, an "Ask Martha" radio show on 330 stations and a magazine with 2.4m readers, publicity costs would wipe out profits.

The scandal comes at an inauspicious time for the company. Its publishing arm, 60% of its sales, is maturing. Television (9%) is suffering declining ratings and the Internet operation (10%) is making heavy losses. Most worrying, up to 90% of the group's profits come from merchandising, largely via Kmart, which has been in bankruptcy since January. The retailer is likely to shut a third of its stores and may renegotiate its licence with Omnimedia.

Many companies are closely intertwined with their founders. Some can survive personal scandal. But Martha Stewart has a unique symbiosis with her company, its brands and her products. With a tainted Ms Stewart on board, it is hard to see how Omnimedia can recover. But without her, it is not clear that the company has any future at all. ■

Unleavened

Martha Stewart Living Omnimedia, share price, \$



Source: Thomson Datastream



Lena Woo
Managing Director
Investment Banking

An Asian telecom wanted
to expand its reach.
(An ambitious calling plan.)
Their dream became our own.

Michael
Managing
Debt C

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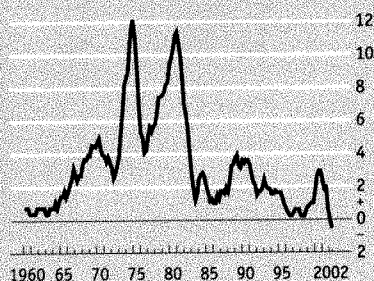
www.morganstanley.com

Even for a rapidly growing telecom, the plan was bold: to become Asia Pacific's #1 telecommunications company. Naturally, they came to Morgan Stanley. We set to work to overcome regulatory and regional obstacles, making a once unthinkable acquisition possible. The result? The company grew significantly. And new lines of communication were opened. Such complex challenges are our passion. Such client successes are our mission. What can we do for you?

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A slow puncture

US price deflator, non-financial business
% change on a year earlier



Source: Bureau of Economic Analysis

► is still over 2%. But Germany's inflation rate is only 1% and it could well drop over the next year, as weaker growth causes its output gap to widen by more than elsewhere. Even if the European Central Bank's (ECB's) monetary policy is appropriate for the euro area as a whole, it is too tight for Germany alone.

As a result, there is a risk that, before the end of 2003, the rich world's three biggest economies—America's, Japan's and Germany's—could all have negative inflation rates. A sharp jump in oil prices as a result of America invading Iraq could, of course, push up headline inflation. But the longer-term impact of higher oil prices would be deflationary, not inflationary. Higher oil prices operate like a tax that depresses growth, so their medium-term impact would be to heighten the deflation risk.

DeAnne Julius, a former member of the Bank of England's monetary policy committee, argued in a recent speech that there is a one-in-three risk of a significant deflationary period in the main economies between now and 2005. But many of today's central bankers, brought up to believe that their job is to fight inflation, seem to be underplaying the risk.

Deflation is much more harmful than inflation. Falling prices encourage consumers to postpone spending in the expectation of cheaper goods tomorrow; they also make it impossible to deliver negative real interest rates if these are needed to drag an economy out of recession. Most dangerous of all is a cocktail of deflation and debt. Deflation pushes up the real burden of debt, while the value of assets linked to that debt, such as house prices, may have to fall even more sharply in nominal terms to return to a fair level. This has already caused severe balance-sheet problems in Japan, and now America and Germany may be at risk: in both countries debts have surged to record levels.

Central bankers in America and Europe—but not in Japan—still have room to cut interest rates. However, the ECB held interest rates unchanged at 3.25% on September 12th. So long as inflation remains above the ECB's target of "less than 2%",

Consumer confidence

Mood swings and downswings**Can consumer confidence predict the cycle?**

"CONFIDENCE obviously matters," Robert Solow, a Nobel laureate in economics, has said, "and it is just as obviously unmeasurable. So it can explain anything." The University of Michigan is willing to cross swords with the Nobel prize-winner on at least part of that claim. It is confident it can measure American consumer confidence. Twice a month it asks 5,000 consumers how they feel about their current finances and future prospects (the Conference Board, a New York-based business club, does a similar survey). Since June, Michigan's index has fallen from 92.4 to 87.6. This week, the first September reading will be closely watched for further signs that American consumers are losing their nerve.

But if some believe confidence can be measured, others doubt it can explain anything. Carl Steidtmann, Deloitte's chief economist, argues that the media, and many economists, give too much weight to consumer confidence. "Consumers don't base their spending behaviour on their hopes and fears," he says. "They base it on their cashflow." With taxes cut, incomes growing, and jobs stable, consumers have money to spend—and spend it they have, boosting retail-sales volumes by 1.1% in July. Consumers may feel glum, Mr Steidtmann accepts, but what counts is how they act. If they keep buying, it doesn't matter whether they see the shopping trolley as half-full or half-empty.

The University of Michigan's Philip Howrey has scrutinised the predictive power of consumer sentiment more carefully. His findings cut both ways. As Mr Steidtmann suggests, once October's figures for personal income are known, consumer confidence will have nothing more to say about fourth-quarter spend-

ing. But those figures will not be out until the end of November. October's confidence reading is available a month earlier. Consumer sentiment is news, Mr Howrey finds, but only until the income figures are released.

Consumer confidence also yields clues about the chances of a recession. It is a better leading indicator of downturns than the stockmarket, and, when combined with stock prices, it says more. In the fourth quarter of 2000, for example, even as Al Gore touted the economy's strength in his election campaign, a forecast based on consumer sentiment and share prices suggested a rising probability of a 2001 recession. More ominously, in the summer of 1981, with the economy growing at over 4% and recession seemingly over, falling confidence gave a strong hint of the double dip to come.

Mr Steidtmann discounts such hints: "We cannot think ourselves into or out of a recession," he insists. Animal spirits, as Keynes argued long ago, may guide the actions of investors, but consumers, the evidence suggests, are still ruled by their wallets.

Popular capitalism may be changing that. Thanks to credit cards, home-equity loans and mutual funds, what consumers have in their wallets depends partly on their willingness to gear up, play the stockmarket, and bet on house-price booms. When their animal spirits flag, consumers may hoard money rather than borrow more. If so, their prudence may bring on the very recession they hoped to cushion themselves against. For Mr Steidtmann, hopes and fears have no economic meaning. But as Keynes's biographer, Robert Skidelsky, has said, "fear of the future can take its revenge on the hopes of the present."

the bank will be in no rush to ease policy. The Fed is also widely expected to keep rates steady at its policy meeting on September 24th. Why wait, when the risks are so lop-sided? Once deflation sets in, monetary policy can do little to revive an economy. If economies perk up and a rate cut turns out to have been unnecessary, it can be reversed: with ample excess capacity, the risk of inflation taking off is low.

Many central bankers do not seem to grasp that this economic cycle is different from its predecessors. The recession was caused not, as before, by inflation taking off, but by the bursting of an asset-price

bubble. American economists blame Japan's deflation on the incompetence of its policymakers. There is some truth in this, but the awkward fact is that post-bubble economies tend to be deflation-prone.

Even with interest rates at zero, Japan might have escaped deflation two years ago, when the American economy was strong, by devaluing the yen. But the world economy cannot pull off that trick. That is why central banks in America and Europe need to heed the danger now. "Deflation is like quicksand," says Dylan Grice of Dresdner Kleinwort Wasserstein; "easy to get stuck in, more difficult to escape." ■

Reinsurance risks

Disaster and its shadow

NEW YORK

Reinsurers are rethinking their risks, and trying to quantify them better

CATASTROPHES have been a hard school for reinsurers. After each disaster, reinsurance companies have tried to improve the way they manage their risks. Hurricane Andrew, which wrought havoc in Florida in 1992, the Northridge earthquake that shook California in 1994, and the windstorms that blew across Europe in 1999 all helped with the learning curve.

Yet the past year's man-made and natural mega-catastrophes have made many reinsurers question why they are in the business at all. The terrorist attacks in America caused the biggest reinsured losses ever. An explosion at a chemical plant in Toulouse last September was one of the costliest industrial accidents in history. And recent floods in Europe will cost reinsurers billions of dollars.

Despite hefty increases in reinsurance premiums when contracts were renewed at the beginning of the year, the industry is not well. In its annual report on reinsurance, released on September 9th, Moody's Investors Service says the outlook for the industry is negative in the near term, citing unprecedented catastrophe losses, poor investment returns and the consequences of the previous low level of premiums. The Financial Stability Forum last week criticised the opaqueness of reinsurance, worrying about the effect of undisclosed problems in the industry on the world financial system.

Moody's lowered the credit ratings of four reinsurers eight months ago. But Patrick Ryan, chairman of Aon, a reinsurance broker, gave warning this week against reinsurers retreating from the market at a time when demand is increasing. Cigna, CNA, Generali, Gerling and Royal & Sun Alliance (all companies that write primary insurance and reinsurance) have partly or entirely withdrawn from reinsurance. Others have either sold or spun off their non-life business, or have plans to do so.

The reinsurers and primary insurers that are still in the catastrophe game have increased their premiums, but they have been excluding more risks and tightening terms and conditions on contracts. Since September 11th 2001, about \$24 billion of new capital has gone into reinsurance, a third of it in Bermuda. But that is still not enough.

Although the industry is going through a rough patch commercially, reinsurers are attempting to quantify more carefully their exposure to catastrophe risk. That

increasingly means the use of computer programs to model probabilities.

Applied Insurance Research (AIR), Eucat and Risk Management Solutions (RMS) are the three biggest risk modellers. Their quantitative measures of risk saw more demand after Hurricane Andrew ten years ago. "Before Andrew everyone assumed the largest probable hurricane loss was \$7 billion," says Karen Clark, AIR's chief executive. AIR had estimated that hurricanes could cause losses of as much as \$30 billion. Within hours of Andrew striking, AIR put the estimated losses at \$13 billion, only a bit lower than the final bill.

Risk models for natural catastrophes try to capture two things: severity (how hard a catastrophe might hit) and frequency (how often it might happen). Severity is calculated by gathering earth-science data—wind-patterns to assess the strength of a hurricane, shifts in tectonic plates to determine the strength of an earthquake. These data are overlaid with estimates of exposure: for example, the number of buildings in an area that are vulnerable and what it would cost to rebuild them. "These models are very good on severity, but frequency is much harder," says Todd Bault at Sanford Bernstein, an investment-research firm. Historical data on catastrophic events are understandably rare. Risk models can only guess at the probability of a strike in a particular place. It is possible, for instance, to say that

there is a 60% chance of a major earthquake in Istanbul in the next 30 years, says Howard Kunreuther at the Wharton School at the University of Pennsylvania. But that does not narrow down the year.

Since September 11th, there has been a new focus on risk-modelling terrorist attacks. Almost all reinsurers at present refuse to write terrorism business. Some would, however, re-enter the market if they understood the probabilities better.

AIR released its risk model for terrorism last week and RMS will follow on September 18th. Both companies worked with counter-terrorism experts from the FBI, the CIA and the Rand Corporation, as well as with experts on weapons systems and asymmetric warfare. They catalogued landmarks to identify potential targets for attacks (AIR found more than 300,000). They are evaluating terrorists' capabilities by, for instance, studying their weapons, and then estimating the cost of a terrorist attack. RMS is also using game theory to model the terrorist mindset. "This is much more challenging than natural-catastrophe models," admits Hemant Shah, chief executive of RMS. As with modelling natural disasters, it is easier to assess severity than frequency.

Many reinsurers are sceptical about modelling terrorist risk. Most prefer old-fashioned prudence, which at present dissuades them from insuring it at all. Whatever the usefulness of the models, the debate may make reinsurers' attitude to catastrophe risk less reactive. RMS is encouraging its clients to take a "holistic" view of their catastrophe risk, rather than writing business too cheaply in the good times, then recoiling irrationally after each unexpected disaster. If reinsurers were mindful of the total catastrophe risk in their portfolio, says Mr Shah, they would be much more prudent. ■



It's happening too often

Citigroup

Passing the buck

NEW YORK

Sandy Weill says Citi should have higher standards

"CERTAIN of our activities do not reflect the way we believe business should be done," said Citigroup's chairman, Sandy Weill, this week. To underline his point, and divert attention from himself as prime architect of Citigroup's complex business edifice, he moved another man sideways: Michael Carpenter, head of Citi's investment bank, Salomon Smith Barney, which is under investigation for dubious business practices.

Mr Weill did something similar in June, displacing Victor Menezes, head of emerging markets, after Citigroup had been caught with a big exposure to a collapsing Argentina. In August, when Citi's former enthusiasm for telecoms shares became an embarrassment, the erstwhile prized analyst behind it, Jack Grubman, found it wise to resign. The bank is still under fire for structured-finance transactions done for Enron, bond underwriting for WorldCom and the curious methodology it used to allocate initial public offerings. It is also negotiating with the Federal Trade Commission to settle charges of predatory lending to retail customers.

Given the heightened risks of prosecution and litigation that threaten Citigroup, Mr Weill's choice of Charles Prince, the group's former top lawyer, to run the investment bank may seem appropriate. But it is more like damage limitation than a drive for higher returns. Expect more changes as performance in other bits of Citigroup's business fails to show Mr Weill in a good light.

Mr Prince's appointment was accompanied by the trumpeting of a new, more virtuous business model. Citi will resolve the conflicts between research and investment banking, file its financial reports sooner, allocate public offerings more fairly, project gains in pension funds more conservatively, treat stock options as an expense, and insist that structured transactions be more clearly disclosed. "No platitude is being left unsaid," commented Kathy Shanley of Gimme Credit, a research boutique. A new "best practices committee", reporting directly to Mr Weill, will ensure that Citi follows the "industry's highest standards". What, it is fair to ask, were the standards before?

Mr Weill has been careful to blame any problems on industry practices and to insist that no laws were broken. But the legal-proceedings section of the company's second-quarter report to the Securities and

Exchange Commission makes sobering reading. On June 30th, eight separate suits were pending over Global Crossing, and 15 over WorldCom. That was before Citi executives were grilled in congressional hearings, bringing out more details of Citi's business practices. These issues may have to be resolved before Citi wins regulatory approval for its \$6 billion acquisition of Golden State Bancorp, a large California thrift that would expand the group's retail-banking business to the West Coast.

Citi's shares are trading at 40% below their latest high. That is despite the flurry of recent announcements, and results which were the envy of Wall Street. In the first six months of the year Citi made almost \$9 billion in profits, shrugging off poor business conditions in America and assorted disasters in Latin America. Return on equity was over 20%. The problem is the future.

Citi faces tighter regulation and the risk that, in a stricter environment, the most lucrative and complex transactions may no longer be feasible, says David Ellison, manager of the FBR Financial Services Fund, a mutual fund. Citi's investment-banking clients, under close market scrutiny, will have to provide so much disclosure that the complexity will not be worthwhile. No outsider can be sure how much of Citi's profits came from such work. The market fears that "best practices" will translate into lower returns and higher risk. Changing that view will take more than a mere management reshuffle. ■

Terrorist finance

Moving target

CAMBRIDGE, ENGLAND

Money launderers keep a few steps ahead of academe

HAD a money launderer or a terrorist financier attended the International Symposium on Economic Crime in Cambridge this week, he might have felt reassured. Despite the symposium's gung-ho title—"Putting the Crooks out of Business!"—the hundred or so police officers, academics, lawyers, regulators and politicians who gather for this meeting every year admit that their quarry is always several steps ahead of them. There is continuing disunity in the international effort against money laundering and terrorist financing. In the corridors, officials complained that many countries still either refuse or prevaricate when asked to cooperate with their investigations.

In previous years, the symposium has tended to tackle issues such as counterfeiting, smuggling and piracy on the high seas.



Now its main subject is terrorist financing. Much progress has been made in the past year, said David Aufhauser, general counsel to the American Treasury and head of a joint agency task-force on terrorist finance. Al-Qaeda is being forced into "neanderthal" conduits such as gold bars and sacks of cash, he said, although it is still raising money from the same old sources—such as drug trafficking and charities.

Disappointingly, given that most of the money which financed the September 11th attacks came through the United Arab Emirates, there was only one speaker from the Arab world, a Kuwaiti. Middle Eastern regulators would have been particularly interested in one of the symposium's subjects: what western countries will do about *hawala*, a trust-based method of moving money that is used by terrorists as well as by expatriate workers in the Gulf and elsewhere. The Treasury's specialist anti-money-laundering body, Fincen, is trying to defend *hawala*, saying that it should be regulated but not pushed underground. It fears, however, that Congress will simply make it illegal.

There was criticism too of America's war on terrorist finance. Countries must deal with terrorism at the political level: "no other method works," said G. L. Pereis, a Sri Lankan minister, who will lead his country's talks with the Tamil Tigers next week. America's anti-terrorist zeal may hurt the innocent, some argued. A lawyer, Wilmer Parker, described the plight of his client, a chicken-plucking firm in north Georgia. After an investigation by America's customs service for connections between its president and an Islamic charity, the company is facing bankruptcy, even though no charges have been brought. Its banks, wary of being accused of financing terrorism, may cut its credit lines. Just because some terrorists use clean money from legitimate businesses, says Mr Parker, the government should not trample on people's constitutional rights. ■

Tokyo commercial property

A fading star

TOKYO

Dazzling office buildings are launched into a dying market

RECSSION? What recession? So visitors must wonder as they take in Tokyo's bustling streets and its skyline, dotted with large cranes. Tokyo has enjoyed a building boom over the past couple of years: office starts tripled between 1998 and 2000. Huge new office complexes are being built in prime central locations. The biggest, due to be completed next spring, will provide more than 2m square metres of new office space (smaller projects are expected to add another 3m square metres).

But demand is falling. There are worries that excess commercial property, dubbed the "2003 office problem", will soon stop Tokyo's mini construction boom and bring down the high occupation rates seen since 2000.

The latest buildings are still luring tenants with their high-tech systems, spaciousness and fashionable designs. One of the swankiest, the new Marunouchi Building—built by Mitsubishi Estate, Japan's second-largest property company—opened for business on September 6th and is already fully occupied. The 37-floor tower, located in the heart of Tokyo's business district, has 160,000 square metres of floor space, housing 140 shops and restaurants and 50 businesses, such as Mitsubishi Securities, its biggest tenant, NTT DoCoMo, Bloomberg and PricewaterhouseCoopers. With other big names moving into three big new developments in Roppongi, Shinagawa and Shiodome next spring, older office buildings are starting to seem unwanted.

That is reversing a trend since the early 1990s when, according to Ikoma Data Service System, a real-estate research centre, vacancy rates in Tokyo started to fall, in fits and starts, from highs of about 9% to 3.6% by early 2001. For big, new buildings in prime locations the rate fell to less than 1%, because of fresh demand from foreign companies and Internet start-ups. Rents in the best bits of Tokyo even went up.

But the end of the Internet bubble and the stockmarket downturn have led foreign investment banks to scale down their operations, or even to move out of Japan altogether. Vacancy rates, 5.1% at the end of June, could rise to 7% next year, predicts Toshihiko Okino, a construction and property analyst at UBS Warburg, an investment bank. Similarly, rents are coming down. Mr Okino reckons they have fallen by about 15% since 2000. Big developments completed last year with pricey

rental targets have had to lower rates to fill their space.

That in turn will hit Tokyo's property prices, which have for the past few years fallen less sharply than in other regions. This is because Japan has adopted an "income approach", a method used in other rich-world countries, which uses rent levels to calculate land prices. Still, Tokyo is unlikely to fare as badly as other areas, which are suffering horribly. For example, vacancy rates are as high as 20% in neighbouring Chiba, and even in Osaka, the second-largest city, they are in double digits. Better transport—a new *shinkansen* (bullet train) stop will open next year in Shinagawa, the site of Tokyo's biggest new development—and struggling regional economies are leading many companies to move even some of their back-office functions back to the capital. ■

Congo's currency

Too many notes

BUKAVU, EASTERN CONGO

Exchange-rate arbitrage favours the brave

FOUR years ago, a new government renamed the country (it used to be Zaire) and launched a new currency, the Congolese franc. The dictator, Laurent Kabila, promised a fresh start after the hyperinflationary binge of his predecessor, Mobutu Sese Seko. Perhaps he should not have given 30 different ministries licences to print money. By 2000, inflation was 511%—lower than under Mobutu, but still dire.



Fresh notes—with the same serial number

Then, last year, Mr Kabila was assassinated. His son and successor, Joseph, stopped the presses. This year, inflation is expected to be about 14%. Mr Kabila junior also ended a rigged official exchange-rate, enforced with the death penalty, that had allowed his father's cronies (but nobody else) to sell francs for greenbacks cheaply and change them back at a 400% mark-up. Things are now better, but still far from normal. Congo is huge (more than six times the size of Germany), divided by a four-year-old war, and has virtually no roads. Rebel-held eastern Congo is cut off from the central bank's printing presses in the capital, Kinshasa, so the notes in circulation, which were once red, pink and orange, are now dirty brown.

Exchange rates vary in different parts of the country. In Kinshasa, the franc trades at about 325 to the dollar; in the east, it is 240; in the area of northern Congo controlled by Jean-Pierre Bemba, a warlord, the rate is 220. Shopkeepers are suspicious of all banknotes anyway, because a previous government once counterfeited its own currency (the official printers printed two or more copies for each serial number, and various cronies kept the duplicates). Traders in the east will accept neither the pink 50-franc note, featuring a humble mud-hut, nor the blue 100-franc note, with its rather grander hydropower station. In the north, all denominations above 20 francs were barred by Mr Bemba, the warlord, until he made peace with the government this year and declared all Congolese notes legal tender in his fief. That includes a relic of the Mobutu era, the new zaire, a gorgeous pink currency, which still circulates in the north at a couple of million to the dollar.

Regional differences in exchange rates are an opportunity for the brave. Army officers buy bundles of francs cheaply in western Congo, smuggle them across the front line, and sell them at a profit. Even UN officials have been implicated: last year, UN ceasefire-monitors were accused of flying bales of cash from Kinshasa to Kisangani, an eastern town, in their taxpayer-financed planes. In general, when the fighting ebbs, as it did after a ceasefire last year, exchange rates tend to converge.

Yet even in Kinshasa the rate remains volatile. One evening last year the franc nearly doubled in value, because a brigade of Zimbabwean soldiers, who were in town to prop up the Congolese government, tried to exchange their dollar pay-packets all at the same time. A peace deal in July between Congo and Rwanda raised hopes of a bit more monetary stability. But Rwanda's troops have not yet quit Congo, and a recent rumour that they plan to make the Rwandan franc legal tender in eastern Congo suggests that they may remain there for quite a while. If so, the chaos will continue. ■

Economics focus The dollar and the deficit

Why the dollar still rules the world—and why the world should be grateful

THE dollar is looking vulnerable. It is propped up not by the strength of America's exports, but by vast imports of capital. America, a country already rich in capital, has to borrow from abroad almost \$2 billion net every working day to cover a current-account deficit forecast to reach almost \$500 billion this year.

To most economists, this deficit represents an unsustainable drain on world savings. If the capital inflows were to dry up, some reckon that the dollar could lose a quarter of its value. Only Paul O'Neill, America's treasury secretary, appears unruffled. The current-account deficit, he declares, is a "meaningless concept", which he talks about only because others insist on doing so.

The dollar is not just a matter for America, because the dollar is not just America's currency. Over half of all dollar bills in circulation are held outside America's borders, and almost half of America's Treasury bonds are held as reserves by foreign central banks. The euro cannot yet rival this global reach. International financiers borrow and lend in dollars, and international traders use dollars, even if Americans are at neither end of the deal. No asset since gold has enjoyed such widespread acceptance as a medium of exchange and store of value. In fact, some economists, such as Paul Davidson of the University of Tennessee and Ronald McKinnon of Stanford University, take the argument a step further (see references at end). They argue that the world is on a de facto dollar standard, akin to the 19th-century gold standard.

For roughly a century up to 1914, the world's main currencies were pegged to gold. You could buy an ounce for about four pounds or twenty dollars. The contemporary "dollar standard" is a looser affair. In principle, the world's currencies float in value against each other, but in reality few float freely. Countries fear losing competitiveness on world markets if their currency rises too much against the greenback; they fear inflation if it falls too far. As long as American prices remain stable, the dollar therefore provides an anchor for world currencies and prices, ensuring that they do not become completely unmoored.

In the days of the gold standard, the volume of money and credit in circulation was tied to the amount of gold in a country's vaults. Economies laboured under the "tyranny" of the gold regime,

booming when gold was abundant, deflating when it was scarce. The dollar standard is a more liberal system. Central banks retain the right to expand the volume of domestic credit to keep pace with the growth of the home economy.

Eventually, however, growth in the world's economies translates into a growing demand for dollar assets. The more money central banks print, the more dollars they like to hold in reserve to underpin their currency. The more business is done across borders, the more dollars traders need to cover their transactions. If the greenback is the new gold, Alan Greenspan, the Federal Reserve chairman, is the world's alchemist, responsible for concocting enough liquidity to keep world trade bubbling along nicely.

But America can play this role only if it is happy to allow foreigners to build up a huge mass of claims on its assets—and if foreigners are happy to go along. Some economists watch with consternation as the rest of the world's claims on America outstrip America's claims on the rest of the world. As they point out, even a dol-

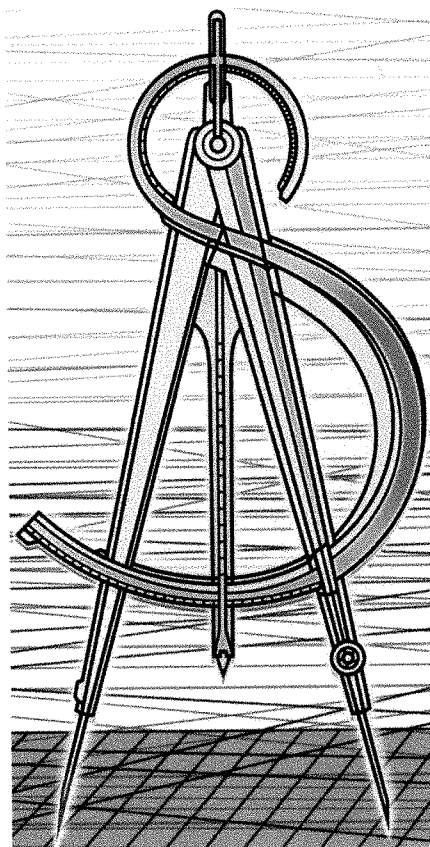
lar bill is an American liability, a promise of ultimate payment by the US Treasury. Can America keep making these promises to foreigners, without eventually emptying them of value?

According to Mr Davidson, the world cannot risk America stopping. America's external deficit means an extra \$500 billion is going into circulation in the world economy each year. If America reined in its current account, international commerce would suffer a liquidity crunch, as it did periodically under the gold standard. Hence America's deficit is neither a "meaningless concept" nor a lamentable drain on world savings. It is an indispensable fount of liquidity for world trade.

Spigot by nature

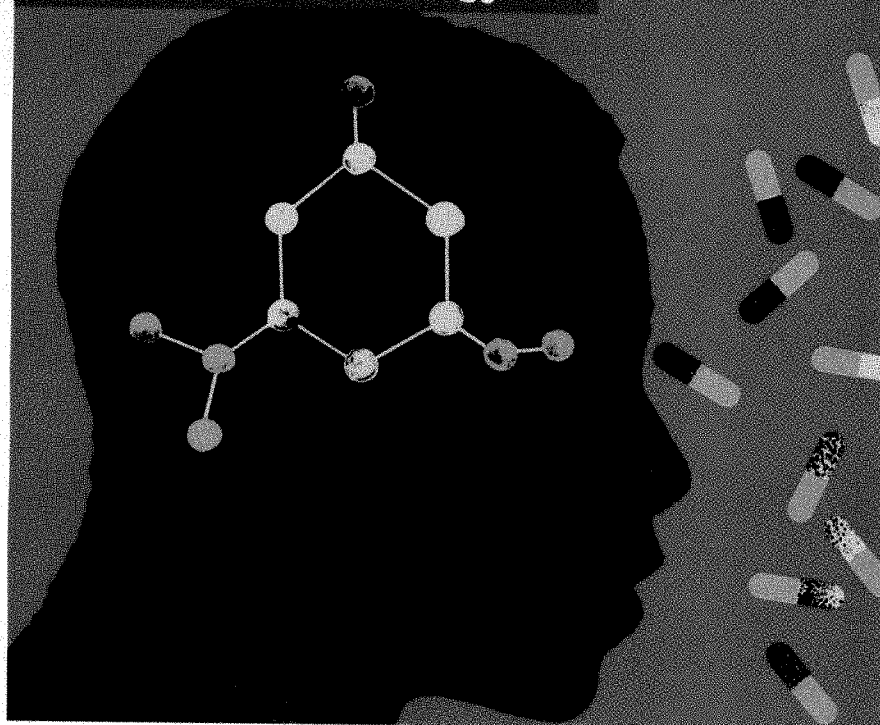
But is the deficit sustainable? Many of America's creditors, Mr McKinnon argues, have a stake in preserving the dollar standard, whatever the euro's potential charms. In particular, a large share of America's more liquid assets are held by foreign central banks, particularly in Asia, which dare not offload them for fear of undermining the competitiveness of their own currencies. "Willy nilly," Mr McKinnon says, "foreign governments cannot avoid being important creditors of the United States." China, for one, added \$60 billion to its reserves in the year to June by ploughing most of its trade surplus with America back into American assets.

This is not the first time America's external deficits have raised alarm. In 1966, as America's post-war trade surpluses began to dwindle, *The Economist* ran an article entitled "The dollar and world liquidity: a minority view." According to this view, the build-up of dollar claims by foreigners was not a "deficit" in need of "correction". Rather, the American capital market was acting like a global financial intermediary, providing essential liquidity to foreign governments and enterprises. In their own ways, Mr Davidson and Mr McKinnon echo this minority view today. A "correction" of America's current deficit, they say, would create more problems than it would solve. Whether the world's holders of dollars will always agree remains to be seen. ■



"Financial Markets, Money and the Real World" by Paul Davidson. Edward Elgar 2002.

"The International Dollar Standard and Sustainability of the U.S. Current Account Deficit" by Ronald McKinnon 2001. Available on www.stanford.edu/~mckinnon/papers.htm



Intellectual property

Patently problematic

An important new study shows the promise, and pitfalls, of intellectual-property rights for the poor

INTELLECTUAL-PROPERTY rights (IPR), which embrace patents, copyright, trademarks and trade secrets, were once considered an esoteric, and slightly dull, bit of commercial law.

No longer. Today, IPR law is the focus of intense interest, and it is not just lawyers who are paying attention. The original purpose of patents was to encourage innovation, and thus growth, by creating an incentive for inventors to disclose the details of their inventions in exchange for a limited monopoly on exploitation. Some argue that the modern system of IPR law is having the opposite effect—delaying the diffusion of new technology.

John Barton, a law professor at Stanford University, wants to see both rich and poor countries start thinking of IPR more as a development tool, and for them to reconsider the notion that strongly protecting the rights of inventors is automatically good for all. For the past year, Dr Barton has chaired the Commission on Intellectual Property Rights, a body of lawyers, academics, a bio-ethicist and an industry executive convened by Britain's Department for International Development to look at how IPR can work to the benefit of the world's poor countries.

The commission's report, published on

September 12th, sets out detailed recommendations for how developing countries should craft IPR to suit their conditions. Its central message is both clear and controversial: poor places should avoid committing themselves to rich-world systems of IPR protection unless such systems are beneficial to their needs. Nor should rich countries, which professed so much interest in "sustainable development" at the recent summit in Johannesburg, push for anything stronger.

All together now

There was a time when countries could go their own way on intellectual-property rights, and introduce legal protection for creators whenever they thought it appropriate. For most of the 19th century, America provided no copyright protection for foreign authors, arguing that it needed the freedom to copy in order to educate the new nation. Similarly, parts of Europe built their industrial bases by copying the inventions of others, a model which was also followed after the second world war by both South Korea and Taiwan.

Today, however, developing countries do not have the luxury to take their time over IPR. As part of a trade deal hammered out eight years ago, countries joining the

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World Trade Organisation (WTO) also sign up to TRIPS (trade-related aspects of intellectual-property rights), an international agreement that sets out minimum standards for the legal protection of intellectual property. The world's poorest countries were given until 2006 to comply in full with the requirements of the treaty.

Contrary to popular perception, TRIPS does not create a universal patent system. Rather, it lays down a list of ground rules describing the protection that a country's system must provide. These extend IPR to include computer programs, integrated circuits, plant varieties and pharmaceuticals, all of which were unprotected in most developing countries until the agreement. Patent rights are valid no matter whether the products are imported or locally produced, and protection and enforcement must be extended equally to all patent holders, foreign and domestic.

Although many poor countries feel that TRIPS gives them a raw deal—all cost and scant benefits—few want to see the agreement dismembered or removed from the WTO, according to Rashid Kaukab, at the South Centre, a think-tank based in Geneva. That is largely for fear of what might take its place. Instead, a few developing countries, such as India and Brazil, are starting to flex their muscles when it comes to the battle between western standards of IPR protection and matters of public interest, such as health and farming. As the commission points out, the wording of TRIPS gives poor countries considerable latitude to look out for themselves when introducing new systems of IPR protection. It also suggests a few ways that they can make the most of this flexibility in a ▶▶

▶ number of important areas:

- **Drugs** Much of the recent debate over the impact of IPR on the poor has centred on the issue of access to expensive medicines. On paper, many of the world's least-developed countries have laws which provide patent protection for pharmaceuticals. In practice, few enforce them. Spurred on by a victory in April 2001 against drug companies fighting patent reform in South Africa, developing countries issued a declaration at the WTO meeting in Doha last year. This asserted the primacy of public health over IPR. They resolved that the world's least-developed countries should be given at least until 2016 to introduce patent protection for pharmaceuticals.

On September 17th, the WTO council responsible for TRIPS will consider a far trickier proposition in the declaration: how to make compulsory licensing (the manufacture and marketing of a patented drug without the patent-holder's consent) work for the poorest. TRIPS already permits compulsory licensing under certain conditions, including national emergencies. This is fine for countries such as Brazil, which have domestic drug industries to copy the medicines. Brazil has, indeed, used the threat of compulsory licensing to wring price discounts out of drug companies, a ploy which the commission, somewhat controversially, supports.

The problem is what to do with countries which have no drug makers. For the moment, they can import generic copies from the likes of India, but come 2006, when those exporters are supposed to have fallen in with the TRIPS line, who will supply the drugs?

- **Education and research** Alan Story, a specialist in IPR at the University of Kent, in Britain, reckons that copyright, particularly as it pertains to education and research, will be the next big battleground. Those countries that have signed up to TRIPS have also accepted international copyright rules. Although these allow some unauthorised copying for "fair use" or personal consumption for education or research, the commission worries that these exceptions are too limited, and that copyright may hamper access to textbooks, journals and other educational material in poor countries, by requiring the consent of, and likely payment to, the publisher prior to copying.

The commission is even more worried about the Internet, which has great potential for broadening access to education in poor countries, but in which encryption technologies can override the principle of fair use. Some publications, such as the *British Medical Journal*, allow free online access for people in poor countries. The commission would like to see more of this. In the meantime, it recommends that developing countries allow users to sneak round technical barriers such as encryp-

tion, to gain access for fair use. Not surprisingly, software makers are unenthusiastic.

- **Traditional knowledge** The most glaring conflict between rich and poor over intellectual property comes from the misappropriation of "traditional knowledge"—such as ancient herbal remedies that find their way into high-priced western pharmaceuticals without the consent of, or compensation to, the people who have used them for generations. Often, patent examiners are simply unaware that the plant variety which an enterprising businessman is trying to patent has been used for centuries by a tribal community half a world away. The commission recommends that countries create databases to catalogue such traditional knowledge (India is already doing so), and urges that consulting such databases should be made a mandatory part of patent examinations the world over.

More than this, however, Kamal Puri, a lawyer at the University of Queensland, Australia, argues that new systems of IPR protection are needed for traditional knowledge. That is because its communal ownership, uncertain date of creation and unwritten form does not fit the requirements of western systems of IPR. On September 17th, a model law, drafted by Dr Puri and co-sponsored by UNESCO, will be unveiled at a meeting of Pacific island states in New Caledonia. The law gives traditional users jurisdiction over native knowledge, and requires that those who wish to commercialise it must seek the users' consent. All transactions must be registered with a tribal authority, which will deal with subsequent disputes.

Even when armed with these weapons, poor countries will have a hard time deploying them. Drafting IPR legislation and setting up a patent office that has modern information-technology systems and trained examiners does not come cheap or easy. Neither does establishing judicial, customs and competition authorities, and police services to enforce IPR rules. The World Bank reckons that it costs at least \$1.5m to create a working system, plus recurrent costs.

Moreover, inventors in poor countries find it tough to use patent systems in the rich world. Merely securing a patent from America's patent office costs at least \$4,000. Defending it in court can cost millions. The commission identifies several ways in which rich countries could open their domestic IPR systems, including discounted fees and subsidised technical assistance. It also suggests they should help poor countries to set up their own systems without saddling them with rich-world standards until they are ready to benefit from them. Inventing a way to do that might be worth a patent in its own right. Those who heed the commission's report, however, might well resist the claim. ■

Nanoelectronics

Small wonders

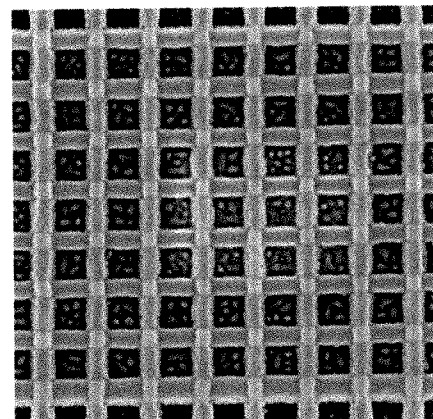
Traditional silicon memory chips are about to face a challenge

SMALL achievements, it seems, are big news these days. Within the past six months, both Hewlett-Packard (HP) and IBM have burst through the silicon ceiling. They have demonstrated circuitry based on radically new technologies that have a much higher density of components than any achieved by today's leading chip manufacturers. This opens up the possibility of storing gigabits of information in an area smaller than a fingernail. And although the two computer-makers' technologies are different, both point towards the end of the age of silicon.

At a meeting of Sweden's Royal Institute of Technology in Stockholm on September 9th, Stanley Williams, director of quantum science research at HP, announced that his group had created the highest density of electronically switchable memory so far. "Electronically switchable" means that each bit of memory can be flipped on and off by a current, without the need for any moving parts.

Earlier this year, an IBM project named Millipede demonstrated even higher potential storage densities. Millipede uses an array of tiny silicon cantilevers, with downward-pointing tips ("feet") that punch indentations into a thin plastic film which moves beneath them. From a manufacturing perspective, though, Millipede may be less attractive than HP's new device, because it contains moving parts and is thus likely to require a higher degree of manufacturing accuracy.

HP's announcement was significant in three ways beyond the question of mere density. The memory bits are made of molecules known as rotaxanes, rather than silicon, making this the first signifi- ▶



Breaking the memory gridlock

▶ cant demonstration of so-called molecular electronics. Second, it demonstrates the reliability of a new contact-printing technique that should allow molecular-electronic components to be printed cheaply. The third advantage is that HP has shown that such components can be read and "written to" in an economic way. Although the demonstration device contains only 64 bits, the tests suggest that scaling up should prove to be straightforward. One square centimetre of such molecular-electronic wizardry should therefore be able to store 6.4 gigabits of information.

The individual bits are not yet single molecules. Each consists of about 1,000 rotaxane molecules trapped in a minute junction between wires made of platinum and titanium. The wires themselves are only 40 nanometres (billionths of a metre) wide. Although HP is also looking at other metal/molecule systems, the wires are so tiny that it is not prohibitively costly to use precious metals.

The memory bits (ie, the ones and zeros of the binary arithmetic used by computers) are written into each cluster of molecules by changing the structure of those molecules. A small voltage is applied across the clusters using current in the metal wires. The resulting change in structure alters the electrical resistance of the molecules by a factor of 10,000—making it easy to measure whether the state of the cluster represents a "one" or a "zero".

Researchers in the field do not yet understand the manoeuvrings that change the molecules' resistance. However, they do know that a phenomenon called quantum tunnelling is involved. During quantum tunnelling, one of many strange physical effects that occur at small scales, electrons spontaneously disappear from one place and reappear nearby.

The components of the circuitry are stamped on to the chip using an inexpensive technique called nano-imprint lithography. A master mould is carved out of silicon, using a precise beam of electrons. The resulting mould is pressed into a layer of polymer, and the trenches created in the polymer are filled with platinum. After that, a single layer of rotaxane is deposited on top and, once the mould has been rotated by 90°, another set of trenches and wires is made on top of the rotaxane.

Perhaps the most important part of HP's announcement is its demonstration of a "logic circuit" for addressing each bit of molecular memory. A logic circuit has several inputs and a single output. It is the physical embodiment of a mathematical equation and, as in an equation, the value of the output depends on the state of the inputs. The practical benefit of this is that any particular bit of memory can be addressed without having to measure the state of every single pair of wires.

One of the advantages of HP's device is

Irritating coins

Allergic to the euro

Why the euro may be a rash move

IT IS not only Eurosceptics who can claim allergy to the euro. Anybody who is sensitive to nickel may also wish to handle the coins with care. Research published in *Nature* this week shows that one- and two-euro coins, when clutched in sweaty hands, release 300 times more nickel than is allowed by EU guidelines. Frank Nestle, a dermatologist at the University of Zürich Hospital, in Switzerland, was prompted to investigate the coins after hearing complaints in his clinic.

Even before euro coins became legal tender in January, there was consternation at the use of nickel alloys in their manufacture. It was argued that nickel ions leaching out of the coins as they

corroded would cause hand eczema in the 15% of women and 2% of men who are already allergic, and might sensitise more of the population to nickel as well. However, the alloys employed in the euros—cupro-nickel and nickel-brass—have long been used to make hard-wearing coins that are difficult to forge. What was good enough for individual EU countries was surely good enough for the common currency.

But the results suggest that euros are worse than the coins they have replaced. The one- and two-euro coins release more irritating ions than a lump of pure nickel would. Dr Nestle worked in collaboration with Hannes Speidel and Marcus Speidel, two metallurgists, to find out why. The problem, they concluded, is the dashing two-tone design. The outer ring and the inner circle are made from different alloys, which have different electric potentials. Clutch a coin in a sweaty hand and the metals connect through the salty solution to make a mini-battery. The tiny current produced is harmless in itself, but the flow of charge drags nickel ions out of the coin and on to the skin.

Stephen Carter, a researcher at LGC, a chemical laboratory in Britain, was asked to test the coins before they were introduced into circulation. He also reported, in a paper published in *Contact Dermatitis* in March 2001, that nickel release from the euro coins exceeded EU guidelines. However, he explains that the exposure limits are for prolonged contact—as with jewellery or a watch. Coins are not usually in the hand for long enough to do any harm when they pass straight from purse to retailer.



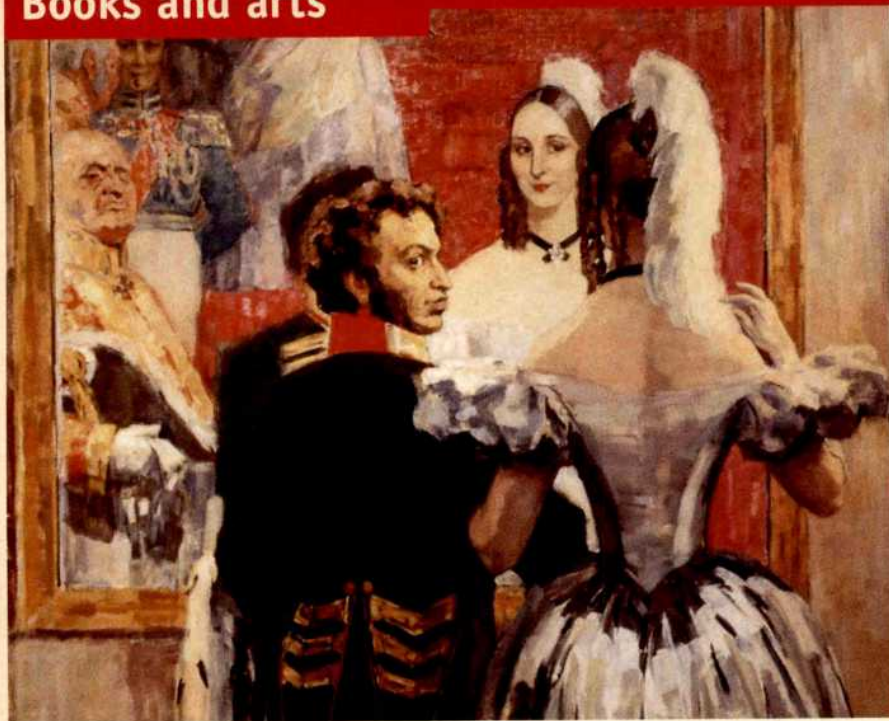
A handful of trouble

that the memory is "non-volatile". In other words, once the switches are flipped they stay that way. So memory will be retained even when the power is shut off. So far, HP's researchers have demonstrated that memory can be kept like this for four months. There is a snag. The switches typically work only 50-60 times before they start to degrade. On the other hand, as Dr Williams points out, with terabits of storage available, it may never be necessary to erase anything.

HP says that its molecular electronics will take a minimum of five years to commercialise. It intends to do it in part by publicly disclosing its results in order to "seed its own competition". Initially, molecular electronics would be aimed at niche mar-

kets such as flash memory for cameras. Ultimately, though, it should compete with DRAM, the most common form of silicon-based memory.

If HP or IBM (or Intel or Motorola, which are also working on molecular electronics) can commercialise their nano-scale devices, the memory-chip industry will leap ahead of predictions for its future based on silicon semiconductors. HP's demonstration has about ten times the density of memory of the best silicon DRAM memory on the market today. With the cost of new fabrication plants for silicon chips running to billions of dollars, a technology that is both better and cheaper than silicon-based memory can be expected to disrupt the status quo. ■



Literary biography

A small man of great stature

A new biography cleans the mythological encrustations from Russia's greatest poet and details a life that was as extraordinary as it was dramatic

Russian writers have been poorly served by biographers in their own country. Their lives may be celebrated in worthy and uplifting volumes, but true biographies are rare. Russian biography originated in saints' lives, as it did in western Europe, but the closely interrelated evolution of religion and literature in Russia left critics with a squeamishness—exacerbated by censorship—about probing the lives of writers. This is particularly true of persecuted poets like Aleksandr Pushkin who acquired almost divine status as martyrs and prophets when they died, often tragically and at a young age.

When, as Russia's Shakespeare, Pushkin was co-opted after the revolution as an icon of Bolshevik propaganda, biography again became hagiography, this time of a political kind. The centenary of Pushkin's death in 1937 marked the zenith of his personality cult, but also its nadir: the purging of several scholars involved in the Academy of Science's edition of his collected works meant publication was completed only in 1949. That even émigré critics should have been shocked by an irreverent essay about Pushkin written by an ex-dissident in the 1970s points to the aura that continued to surround his name long after the end of Stalinism.

How refreshing, then, to read a straight-

Pushkin: A Biography. By T.J. Binyon. HarperCollins; 731 pages; £30

forward, scholarly account of Pushkin's life informed by all the best qualities of English biographical writing and free of ideological constraints. Scrupulously researched, lucidly and objectively written, with an admirable lightness of touch and a good dose of dry humour, T. J. Binyon's "Pushkin" deserves to join other English biographies that are being translated into Russian.

The author will be a dark horse to those who know him only from his frequent reviews of detective fiction. But Mr Binyon, a teacher of Russian at Oxford University, has finally redeemed his debt to the literature he actually lectures in. Although his book came too late to coincide with the bicentenary of Pushkin's birth in 1999, it has been worth the wait.

Standing no more than five feet (1.5m) tall, Pushkin may have been short of stature physically, but in literary terms he was a giant. The first world-class writer to emerge in Russia, and the author of the first Russian novel, "Eugene Onegin" (albeit in verse), Pushkin wrote in every conceivable genre, and often with an irony that seems astonishingly modern to the

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contemporary reader. He is renowned as the founder of the Russian literary language, but the deceptively simple lines of his poetry (whose expressive power and finesse have been compared to the music of Mozart) have proved notoriously difficult to translate. It is for this reason that Russia's undisputed national poet is not better appreciated outside his homeland.

Mr Binyon's work follows the trajectory of the poet's life in conventional fashion, his crisp chapter headings—"Ancestry and Childhood, 1799-1811", "In Search of a Wife, 1826-29", "The Tired Slave, 1833-34"—suggesting something of the businesslike way this biography has been tackled. Mr Binyon does not use the life to explain the works. With the exception of "Eugene Onegin", which is both a parody and a prophecy of his own destiny, Pushkin's protean writings are mentioned only in passing. Few of his celebrated lyrics are cited, and then usually in connection with an infatuation, of which there were many.

Mr Binyon's focus instead is on the minutiae of the day-to-day life of the poet, who does indeed emerge here as a rounded and complicated human being. This is no mean achievement. The curly-haired great-grandson of impoverished Russian aristocrats and an Abyssinian boy given to Peter the Great, Pushkin was a down-to-earth, outspoken man with long fingernails and slovenly habits who liked to write best of all in bed. Despite having what he called a "monkey's face", he enjoyed numerous amorous liaisons before his marriage, fuelling an uninhibited erotic imagination that expressed itself in reams of unpublished verse.

There were also few outlets for his wit and erudition, and even the reader ac-

► acquainted with the bare outlines of Pushkin's biography (privileged upbringing, rebellious youth, exile, personal censorship by the tsar, marriage to a society beauty, untimely death in a duel) will be struck by the suffocating lack of creative freedom so vividly conveyed here. Pushkin's personal correspondence was intercepted, his movements monitored and his life closely tied to that of the court. Not only did Tsar Nicholas I's decision to oversee his career oblige him to submit all his manuscripts for inspection, but his perennially desperate finances entailed humiliating negotiations with the tsar's chief of secret police over his loans. And when Pushkin's wife caught Nicholas's eye, the increasingly beleaguered poet was coerced into becoming a junior courtier so that she could attend all the right balls.

The recklessness with which Pushkin fought duels and even gambled away some of his own manuscripts is no doubt directly attributable to the need to assert some kind of independence in such a repressive world. Although Mr Binyon provides pithy explanations where necessary, the profusion of Russian names and places may seem bewildering and it is best to come to this biography with at least a rudimentary knowledge of Pushkin's life and work. That said, the long final chapter recounts with true Pushkinian detachment the machinations of Georges d'Anthes, the unscrupulous Frenchman who was the cause of the poet's wasteful death, at the age of 37. It makes for a gripping end to an impressive work. ■

New British fiction

Good bad and plain bad

The Autograph Man. By Zadie Smith. *Random House*; 400 pages; \$24.95. *Hamish Hamilton*; £16.99

Behindlings. By Nicola Barker. *Flamingo*; 534 pages; £10.99. To be published in America by *Ecco Press* in December

HAD enough of novels that make obvious sense? Books with a conventional plot? Stories that actually go somewhere? Characters you can relate to? Then try the latest offerings from Zadie Smith and Nicola Barker. They are probably two of the most frustrating novels you will read this year.

"The Autograph Man", a follow-up to Ms Smith's smash debut, "White Teeth", is an uneasy mix of "Sunset Boulevard" and J.P. Donleavy's "The Ginger Man". The cast revolves around Alex-Li Tandem (the 27-year-old son of a Jewish mother and Chi-



When things were looking up

nese father), his frustrated couplings with Esther (who wears a pacemaker that he likes rubbing between his thumb and forefinger), his search for religious certainty among the minutiae of the Kabbalah and Zen Buddhism, and his career as a collector, verifier and occasional forger of celebrity autographs.

The real love of Alex-Li's dementedly self-absorbed existence is the novel's Norma Desmond, a reclusive former screen beauty named Kitty Alexander. Alex-Li's quest for her rare signature takes him and many bizarre hangers-on to a series of autograph auctions, which form the backdrop to this endless, and endlessly weird, adventure.

"The Autograph Man" is neither properly picaresque nor, despite the boast in the cover blurb, terribly funny. The characters are shrill, cartoon-like figures, and the bubblegum text is so distended with italics, capital letters, lists, diagrams, poor jokes and faux parables that you end up wanting to stick it to the underside of your chair and leave it there.

"Behindlings", Ms Barker's fourth novel, concerns a weird, grotty fellow called Wesley; some kind of practical joker, apparently, whose slightly sinister antics have earned him a band of groupies, or "behindlings", who follow him devotedly on his peregrinations around Canvey Island in the Thames estuary. As well as the various behindlings, there's another character, Katherine Turpin, whom Wesley has wronged in the past, though it's never clear exactly how. (There are allusions to the theft of an antique fishpond.)

Ms Barker won the IMPAC prize for her previous novel, "Wide Open". She certainly writes well. But "Behindlings" is maddeningly bereft of most of the ordinary pleasures of the novel. Instead, it's full of stream-of-consciousness ramblings and interminable descriptions of the grim Can-

vey landscape. Take a couple of examples. "Then finally, the refineries. Balanced on the coastline like a clutch of steel reptiles. Like iguanas, nodding complacently—perhaps in friendship, possibly in challenge—towards the hoary, pewter, slate-smashed sea. Dry-clawed, shining, harsh, bulbous, slithering, contained, pristine." A few pages later a character throws a key into the water. "He diligently supervised its multiple adventures—its brief spiralling rise, its determined fall (like a sycamore seed, a helicopter blade, an injured grouse on the wing), its eventual splash-landing, its half-hearted floating, its gradual submerging, with a strong, with a wicked, with a powerful sense of satisfaction."

Why settle for a descriptive phrase when a whole prose-poem will do? This constant elaboration is what pads the book out to such length. But whereas Ms Smith has written a bad book badly, Ms Barker has written a bad book with tremendous style and individuality. The main problem with "Behindlings" has to do with excess: it's too long, too woolly, too teasingly obscure. Yet it is full of gorgeous prose, and might well have made an intriguing short story.

"Behindlings" is a failure, but the quality of the writing confirms Ms Barker as a genuine talent. Zadie Smith's "The Autograph Man" is just a failure, and while it is true that this is a second novel and second novels are probably the hardest to write, it would seem only to confirm, sadly, that all the fuss about Ms Smith may have been seriously misplaced. ■

New Irish fiction

Lost and lovely

The Story of Lucy Gault. By William Trevor. *Viking Press*; 288 pages; \$24.95. *Penguin Viking*; £16.99

IN THE sinister world of William Trevor's last two novels, "Felicia's Journey" and "Death in Summer", child abductors and murderers lurked below the glassy surface of his prose. His new book has a less twisted undertow. If Mr Trevor deals in good and evil, redemption here rather than damnation is the keynote.

It begins in Ireland in 1921. Captain Gault, last in line of a Protestant Ascendancy family, fires a shot at three youths bent on an arson attack at his country house. One is wounded, and the Gaults decide to leave their ancestral home. Lucy, their nine-year-old daughter, distraught at the prospect, runs away. Instead of being found and scolded as she expects, she breaks her ankle in the woods. Mean-►►

while, her clothes which she lost on a secret swimming expedition a while back, are found on the seashore. Her grief-stricken parents, believing her to have drowned, leave for Europe and cut all ties with home. By the time the half-starved Lucy is discovered, the incompetent local lawyer is unable to trace them.

Lucy grows up, hermit-like, in the old house with two loyal family retainers who remain there. She works her way through the books in the library, embroiders and communes with nature, while her unknowing, exiled parents wander through Italy and Switzerland. At 21, her isolation is broken by the arrival of a young man with whom she falls in love, but her sense of

guilt and belief that her life must remain on hold until her mother and father return make her reject his proposal. Meanwhile, we follow the descent into madness of the boy who was shot, who is also tormented by guilt at the consequences for the Gaults of his actions. Late in life, he and Lucy meet. Her visits to his asylum offer them both some sense of closure, "the gentle fruit of such misfortune's harvest".

Mr Trevor's writing here is gentle too, with an elegiac elasticity very different from the tense feel of "Felicia's Journey". That novel had all the horror of "Bluebeard". This one is also, at root, a fairytale, but a kindlier fable of loss and longing lit by moments of rare beauty. ■

discussed before his death? Jonathan Wright speculates intelligently on these counterfactuals at the end of his fine new biography. He offers a hard-headed verdict, pointing out the constraints within which a surviving Stresemann would have operated. They included a fragile political base within his own splintered and self-destructive German People's Party, a group of centre-right liberals which supported him with reluctance even during the relatively prosperous mid-1920s when Stresemann was scoring his greatest diplomatic achievements.

Stresemann was the youngest child of a lower middle-class family in Berlin. Like Matthias Erzberger, a leader of the Catholic Centre party, he was one of the new men from modest backgrounds who came to prominence in Wilhelm II's Germany. Mr Wright is excellent on this new generation of professional politicians who lived, in Max Weber's terms, from rather than for politics. After writing a dissertation on the bottled-beer industry, his father's business, Stresemann started in politics organising the Saxon chocolate manufacturers against the powerful sugar cartel. It was a perfect introduction to the rancorous interest politics that bedevilled German liberalism before and after the first world war.

Stresemann rose initially in the National Liberal Party, where his interest in domestic reform coupled with imperialism made him typical of his generation. A fervent annexationist during the war, he then faced a difficult adjustment to defeat and revolution. During the attempted Kapp putsch in 1920 Stresemann remained equivocal about defending the new regime. A major part of this book is taken up with explaining how the critic of the Weimar republic and the Versailles treaty turned into a committed democratic politician and advocate of détente.

Partly, he saw no alternative. He was a *Vernunftrepublikaner*—a believer in the republic on pragmatic grounds rather than from deep conviction—as well as an instinctive consensus-builder ("I incline by nature much more to conciliation than to conflict.") But Mr Wright argues that Stresemann developed a genuine emotional attachment to the republic, which was strengthened by the right-wing assassination of Walter Rathenau.

Pragmatism-plus is also Mr Wright's explanation for Stresemann's policies as German foreign minister, a post he held from 1923 until his death. The Dawes plan, the Locarno treaty and German entry into the League of Nations were all the work of a statesman who had seen the bankruptcy of the alternative during the French occupation of the Ruhr in 1923. The book argues that Stresemann's talk of peace and European economic integration developed into something more than *Realpolitik*. Mr Wright is fair to the arguments made by ►►



German history

Could he have saved Weimar?

Though little known today, he was one of the 20th century's great might-have-beens

GUSTAV STRESEMANN, Germany's foreign minister, died in early October 1929, just weeks before the Wall Street crash that gave Hitler his opportunity. An estimated 200,000 people watched his funeral procession in Berlin and Count Harry Kessler noted in his diary, "It is an irreparable loss whose consequences cannot be foreseen." The sense of shock was equally great outside Germany. Aristide Briand, Stresemann's ally in the Franco-German rapprochement of the 1920s, reportedly said, "Order a coffin for two."

Stresemann's premature death from a stroke—he was only 51—presents one of the great what-if questions in modern Ger-

Gustav Stresemann: Weimar Politician and Statesman. By Jonathan Wright. Oxford University Press; 592 pages; \$35 and £30

man history, like the death of the liberal-minded Kaiser Friedrich III in 1888 after a 100-day reign. Stresemann was, after all, younger than Konrad Adenauer. Could he have prevented the Weimar political system from buckling in the face of National Socialism? What if Stresemann, not the conservative Hindenburg, had become the candidate of the democratic parties in the 1932 presidential elections, a possibility he

► Stresemann's critics. He notes the differences between German policy towards the western and eastern frontiers, and recognises that the dissonance between the two halves of Stresemann's policy—*détente* and revision of Versailles—was growing after 1925-26. Yet his overall judgment echoes that of Austen Chamberlain, who thought that, by degrees, "Stresemann became a convert to his own policies."

Another British commentator, Claud Cockburn, saw it differently: Stresemann had "discovered that the way to get away with being a good German was to pretend to be a good European." Mr Wright rejects this while noting the parallel with debates over German *Ostpolitik* after 1945. His well-documented, carefully argued book is a major contribution to our understanding of Stresemann and of German foreign-policy interests in the 20th century. ■

Film festival

Nuns, Chechens and Aborigines

VENICE

The right films won, mostly

THE jury at the Venice film festival gave its prizes with care this year, rewarding passion more than bluster, and human feeling more than skill, though it did miss two remarkable films.

One was "The Tracker", by a Dutch-born, Australian-based director, Rolf de Heer, who made his name in Venice nine years ago with "Bad Boy Bubby". Mr de Heer's new film, described by some as a western in the outback, is set in 1922 and features a three-man mounted posse hunting for an Aborigine, alleged to be a murderer. They are led, on foot, by an Aboriginal guide, played by David Gulpilil, an actor, dancer and musician imbued with all the quiet charisma of a cinematic Nelson Mandela.

Early on, one of the posse is speared by an unseen hand. A second, an arrant racist, retaliates by slaughtering many of the tribesmen they meet. The third one ends up chastened, like the audience. What lingers, apart from vicarious guilt, is the memory of a vast landscape, bristling with menace, that has to be scanned like a Jacques Tati film for small details, tiny movements, sudden threats.

No less accomplished in a quite different vein is Patrice Leconte's "L'homme du train". The man from the train is a rough-neck played by Johnny Hallyday, a French pop star with a lined face and highlights in his hair. He has arrived by night in a small French town where he plans to rob a bank.

In its deserted streets he encounters an elegant retired teacher, the fine-drawn Jean Rochefort, who lives alone in his late mother's old dark house. The teacher hankers for adventures he never had. The robber seeks refuge and is wistful for the education he lacked. Improbably, they strike up a friendship which lasts, or seems to last, beyond the film's double climax—botched robbery and the teacher's triple-heart-bypass surgery. Mr Rochefort draws on his recent experience of illness to evoke a subtle, delicate relationship between men of different strengths. For this performance he really should have won the award for best actor that went instead to Stefano Accorsi, playing Dino Campana, an insane Italian poet, in an opulent true-life romance, "A Journey Called Love", whose plot, acting and music make Puccini seem like a minimalist.

Still, the Venice jury gave at least one deserved acting prize, for young performers, to Moon So-ri, an exquisite Korean beauty who played a young woman suffering from cerebral palsy in love with a retarded youth in Lee Chang-dong's "Oasis", for which he won the special director's award. The scene in which the girl's deformity dissolves as she dances with her lover was especially touching.

Just as memorable were the psychiatric patients in Andrei Konchalovsky's "Dom Durakov"—(The House of Fools)—which won the jury's second big prize. A return to form after some of Mr Konchalovsky's recent American work, the film recalls the best of those made by his brother, Nikita Mikhalkov. It portrays a run-down mental hospital on the Russian-Chechen border, swept into the larger madhouse of war. The staff flees the double bombardment. Troops from both sides invade and search the premises. One of the more stable patients believes she has fallen in love with a reluctant soldier. He responds, but only

faintly—until he sees in the asylum a true refuge from the war. At first, the actors playing the inmates seem over the top; in fact, most of them were actual patients. In its triple setting—isolation, incarceration and invasion—their plight is remarkably well evoked.

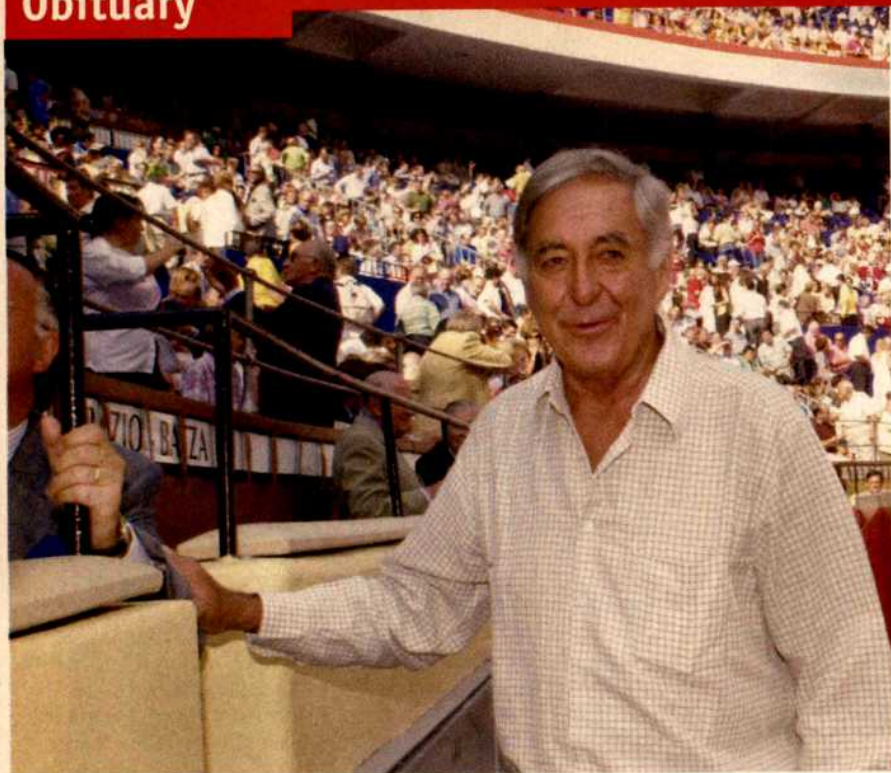
Raw emotion thus transcended the collective art of film making. And the Venice jury felt it from the start. In the first two days of the festival, when less compelling work tends to be screened, one film transfixed every kind of audience. This was Peter Mullan's "The Magdalene Sisters". Fiction based on fact, it rightly won the Golden Lion award.

Its setting is one of the Magdalene asylums set up in 19th-century Ireland by the Catholic Sisters of Mercy as refuges for so-called fallen women. Their good intentions paved the road to Dickensian workhouses, if not to hell. By 1996, when the last one closed, countless women had endured the torment suffered during the 1960s by the young women in the film—one a rape victim, two unmarried mothers parted from their children, and a poor orphanage girl just too pretty for her own good. Shunned by their families, imprisoned, badly fed, forced to work as unpaid laundresses in rough uniforms ten hours a day, seven days a week, the survivors confirm the truth of the story Mr Mullan tells.

Although best known as an actor in Ken Loach's "My Name is Joe", Mr Mullan has proved that he is also a sensitive writer and director with a gift for turning out flawed heroines and believable villains. When *L'Osservatore Romano*, the Vatican's semi-official mouthpiece in Italy, predictably attacked the film, Mr Mullan calmly pointed out that cruel, self-righteous bigotry, contempt for women and a terror of the power of sex are not unique to the Roman Catholic church. Which may be why his film has such universal appeal. ■



Cruelties of the cloth



Manolo Chopera

Manolo Chopera, tycoon of bullfighting, died on September 6th, aged 75

IT WAS a puzzle to Manolo Chopera that anyone should object to bullfighting. Was it not part of Spanish culture? When non-Spaniards continued to be unpersuaded, Mr Chopera would dig deeper into history. Bullfighting had played a part in the very foundations of European culture. Think of the story of the Minotaur, the creature with a bull's head and a man's body, which had the unfortunate habit of eating people until it was killed by Theseus. Was that not an early example of bullfighting?

Mr Chopera would be heard out, usually politely, but he rarely won over opponents to bullfighting. The ceremony of killing the bull is either loved or loathed. There is no middle way. Ernest Hemingway became its most famous supporter in the Anglo-Saxon world, calling it an art: "not a sport but a tragedy". But he was already hooked on violence before he saw his first bullfight, and anyway admired just about everything about Spain. An earlier American writer, Mark Twain, was just as ferociously opposed to the bullring. In a bitter story, bereft of his usual good humour, Twain has a character saying of a Spanish bullfight: "Well, it is perfectly grand, perfectly beautiful. Burning a nigger don't begin."

At least at home Mr Chopera did not

have to be on the defensive. There is some opposition to bullfighting in Spain but set against that is its huge popularity. Critics of bullfighting sometimes claim that it is kept going only because of the support of curious tourists. But the reality is that in most towns with bullrings the number of local supporters is rising.

These days audiences include many women shouting their encouragement to the matadors in their gold-trimmed suits, stockings and white shirts. Jesulin de Ubrique, a matador much admired for his bold style, appeared in a *corrida* staged one evening exclusively for women. Some 9,000 packed the stadium and saw six bulls killed. Purists were appalled. The bullfight was supposed to be a re-enactment of the traditional contest between man and beast, not a kind of pop concert. Was this the way the bullfight was going? If it were, Mr Chopera could take some of the credit, or blame.

Only the best

Nearly all the bullfighting in Spain, and much of it in Latin America, was under the control of Manolo Chopera. He promoted the careers of the top matadors and saw that they fought only the best bulls. For some 30 years wherever bulls were ritually put to the sword Mr Chopera was the

impresario: in the Basque region or in southern Spain around Seville; in Mexico, Venezuela, Ecuador and Peru (where Pizarro, the Spanish conqueror, is said to have dispatched the country's first bull in 1540). He owned Las Ventas in Madrid, perhaps the most important bullring in the world, which seats 25,000 spectators with a box for royalty, and has an operating theatre for matadors who misjudge the bull's cunning and a small chapel for those beyond help.

His father, Pablo Martinez, bred horses for picadors, the horsemen who take part in the preliminaries of a bullfight before the matador appears, provoking the bull to attack them. For generations the Martinez family had bred the heavily-built horses, but now he feared that bullfighting would decline as Spain was being rebuilt after the civil war. He sent his son to France where he gained a degree in chemical engineering at Toulouse university. Manuel Martinez, as he then was (Manolo Chopera is an untranslatable slang name everyone called him), had little enthusiasm for engineering and preferred to work with horses. When his father died in 1968 Mr Chopera took over the business and from it created an empire of blood and sand.

Some critics said that bullfighting flourished in Spain because the country was backward under General Franco, the Spanish dictator until his death in 1975. But Mr Chopera said that blood sports were popular in all countries, poor or rich. You might expect cock fighting to be popular in a poor country such as the Philippines, but it was also tolerated in three states of America. Hollywood films such as the Oscar-winning "Gladiator" fed the lust for blood. In England, Parliament had not been able to stop foxhunting. Highly-paid football stars in Britain roused the crowd with brutal, and damaging, attacks. The spectacle might be nasty but it was human.

Mr Chopera rejected a proposal that Spain should make bullfighting more humane. In Portugal it is illegal to kill the bull in the ring. Promoters in other countries have tried to introduce "humane" bullfighting, among them Russia where the gentle Slavs said it still sounded cruel. Mr Chopera agreed. The bull died anyway, off-stage, while the matador was deprived of his prize. Better to accept that humans were hunters, carnivores at the top of the food chain who enjoy a steak.

The obsequies for Manolo Chopera have been many and ornate. It was noted by some that he died at around six in the evening, just as the day was cooling and the crowds were taking their seats in Las Ventas. With perfect timing the man who had made the show possible would be present in spirit to check all was in order. It sounds mawkish, but perhaps not if you are a bullfighter. ■

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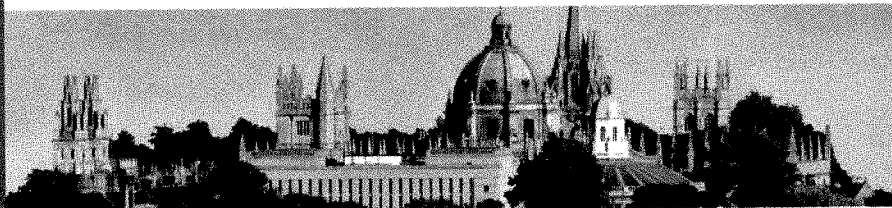
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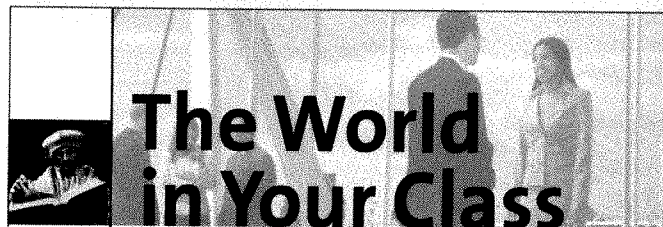
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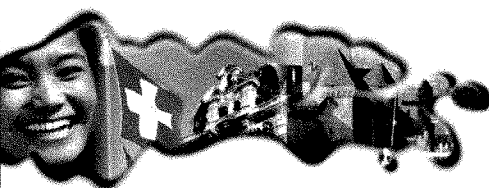
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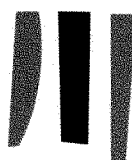
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Forest Economist

You'll offer a needed macro-economic policy perspective to our work – focusing on decentralisation and the private sector and particularly concentrating on due diligence and best practice. You'll also take on policy work in forestry restructuring including downsizing the wood processing industry. Further, you'll contribute to our focus on illegal logging and the trade of illegal timber, and forest finance, nationally and internationally. Your main activity will consist of networking and identifying partners, and developing existing relationships. Providing specialist advice will also be part of your remit.

You'll need a Masters degree in Economics or Natural Resource Economics – and at least ten years' professional experience in forest or natural resource management policy research and advice. Practical experience of livelihood concerns of the forest dependent poor is highly desirable as is understanding of forest policy and management issues in Indonesia. Basic knowledge of multi-stakeholder processes and participatory forest management will be important and ideally, you'll offer some knowledge of Bahasa Indonesia. Language training may be provided so an ability to demonstrate an aptitude to work in different languages would be an advantage.

Communications and Information Technology Specialist

You will have skills in managing local area networks and developing and implementing communication strategies for geographically dispersed teams. You'll ensure we're able to produce relevant information and communicate

directly with, and influence key policymakers. You'll provide technical support specifically on communication and information – implementing, reviewing and developing our ICT strategy, identifying underlying issues, themes and mechanisms, and developing our IT and communication systems. Intranet and Internet offerings will also fall under your lead and you'll manage all sub-contractors and train programme staff and partners to ensure high standards.

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Overview

America's unemployment fell to 5.7% in August, from 5.9% in July. But the labour market remains weak, with no growth in private-sector jobs in the past two months.

GDP in the **euro area** grew at an annual pace of only 1.4% in the second quarter. Industrial production fell by 2.0% in Germany in the year to July; in Spain, it grew by 1.8%. Germany's trade surplus rose above \$10 billion in July, lifting its 12-month surplus to \$104.5 billion.

Japan's GDP growth in the second quarter was revised up from 1.9% to 2.6% at an annual rate. Retail sales fell by 4.8% in the year to July. Meanwhile, producer-price deflation slowed to 1.3% in the year to August.

In **Britain**, the number of people claiming unemployment benefit fell to 943,300 in August, its lowest for 27 years. But the government's preferred internationally comparable measure of unemployment rose to 5.2% in the three months to July.

The prospect of war with Iraq pushed **oil prices** briefly over \$30 a barrel at mid-week. Yet world **stockmarkets** regained much of the ground recently lost. The Dow Jones Industrial Average rose by 1.9% over the week. France's CAC 40 surged by 7.2%.

The **dollar's** trade-weighted value rose by 1.7%; the euro and the yen each fell by just over 1%.

Data on more countries are available to subscribers on www.economist.com

Output, demand and jobs

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production latest	Retail sales (volume) latest	Unemployment % rate	
	1 qtr*	1 year	2002	2003			latest	year ago
Australia	+ 2.4	+ 3.8 Q2	+ 4.0	+ 3.7	+ 4.3 Q1	+ 6.3 Q2	6.2 Aug	6.8
Austria	+ 0.3	- 0.6 Q1	+ 0.9	+ 2.4	+ 2.5 Jun	- 0.2 May	4.2 Jul	3.6
Belgium	+ 0.8	+ 0.3 Q2	+ 1.1	+ 2.7	- 4.1 Jun	- 4.2 Jun	12.0 Aug†	11.6
Britain	+ 2.4	+ 1.2 Q2	+ 1.7	+ 2.9	- 2.5 Jul	+ 4.5 Jul	5.2 Jul‡	5.1
Canada	+ 4.3	+ 3.2 Q2	+ 3.3	+ 3.4	+ 1.3 Jun	+ 6.3 Jun	7.5 Aug	7.3
Denmark	+ 4.4	+ 2.2 Q2	+ 1.6	+ 2.3	- 1.6 Jul	+ 4.1 Jun	5.1 Jul	5.1
France	+ 2.0	+ 1.0 Q2	+ 1.3	+ 2.6	nil Jun	- 2.5 Jun	9.0 Jul††	8.7
Germany	+ 1.1	+ 0.1 Q2	+ 0.6	+ 2.2	- 2.0 Jul	- 1.7 Jul	9.9 Aug§	9.3
Italy	+ 0.9	+ 0.2 Q2	+ 0.8	+ 2.4	- 5.4 Jun	- 0.8 Jun	9.0 Apr	9.5
Japan	+ 2.6	- 0.7 Q2	- 0.5	+ 1.0	+ 3.3 Jul	- 4.8 Jul	5.4 Jul	5.0
Netherlands	+ 0.5	+ 0.1 Q2	+ 0.9	+ 2.4	- 3.0 Jun	- 2.1 May	2.4 Jul**	2.0
Spain	+ 1.8	+ 2.0 Q2	+ 2.0	+ 2.9	+ 1.8 Jul	na	11.3 Jul	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.8	+ 2.7	- 1.3 Jun	+ 4.7 Jul	4.3 Jul†	4.2
Switzerland	+ 0.7	+ 0.2 Q1	+ 0.9	+ 2.2	- 8.8 Q1	+ 1.7 Jul	2.7 Aug†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.5	+ 3.0	+ 0.2 Jul	+ 6.3 Jul	5.7 Aug	4.9
Euro area	+ 1.4	+ 0.6 Q2	+ 1.0	+ 2.4	- 1.2 Jun	- 0.9 Jun	8.3 Jul	8.0

*% change at an annual rate. †Not seasonally adjusted. ‡May-July; claimant count rate 3.1% in Aug. §EU harmonised rate 8.3% in Aug. **May-Jul. ††Revised series.

Prices and wages

% change on year ago

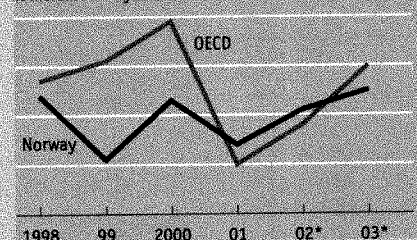
	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2002	2003	latest	year ago	latest	year ago
Australia	+ 2.8 Q2	+ 6.0	+ 2.8	+ 2.5	- 1.1 Q2	+ 5.6	+ 3.7 Q2	+ 4.4
Austria	+ 1.6 Jul	+ 2.8	+ 1.7	+ 1.7	- 0.6 Aug	+ 1.7	+ 2.4 Jul	+ 2.8
Belgium	+ 1.3 Aug	+ 2.7	+ 1.7	+ 1.5	- 0.2 Jul	- 0.4	+ 2.6 Q2	+ 2.6
Britain	+ 1.5 Jul	+ 1.6	+ 1.9	+ 2.4	+ 0.3 Aug	+ 0.2	+ 4.0 Jul	+ 4.6
Canada	+ 2.1 Jul	+ 2.6	+ 1.8	+ 2.2	- 0.3 Jul	+ 0.8	+ 3.0 Jun	+ 1.5
Denmark	+ 2.3 Aug	+ 2.5	+ 2.3	+ 2.0	- 0.9 Jul	+ 2.7	+ 3.7 Q2	+ 4.7
France	+ 1.6 Jul	+ 2.1	+ 1.8	+ 1.4	- 1.5 Jun	+ 2.3	+ 3.8 Q2	+ 4.2
Germany	+ 1.1 Aug	+ 2.6	+ 1.4	+ 1.2	- 0.8 Jul	+ 2.2	+ 2.5 Jun	+ 1.9
Italy	+ 2.3 Aug	+ 2.8	+ 2.3	+ 1.8	+ 0.1 Jul	+ 1.3	+ 2.2 Jul	+ 2.5
Japan	- 0.8 Jul	- 0.8	- 0.9	- 0.5	- 1.3 Aug	nil	- 5.6 Jul	+ 0.7
Netherlands	+ 3.3 Aug	+ 4.7	+ 3.6	+ 2.4	- 0.4 Jul	+ 2.4	+ 3.0 Jul	+ 5.1
Spain	+ 3.4 Jul	+ 3.9	+ 3.3	+ 2.6	+ 0.6 Jul	+ 2.0	+ 4.0 Q1	+ 3.4
Sweden	+ 2.2 Jul	+ 2.9	+ 2.3	+ 2.0	- 0.8 Jul	+ 2.1	+ 2.9 Jun	+ 2.8
Switzerland	+ 0.5 Aug	+ 1.1	+ 1.0	+ 1.2	- 1.6 Jul	+ 0.2	+ 2.5 2001	+ 1.3
United States	+ 1.5 Jul	+ 2.7	+ 1.6	+ 2.2	- 1.1 Jul	+ 1.4	+ 3.1 Aug	+ 4.1
Euro area	+ 2.1 Aug	+ 2.7	+ 2.1	+ 1.6	- 0.6 Jul	+ 2.1	+ 3.3 Q1	+ 2.8

Norway

High oil prices have given Norway a huge current-account surplus. Assuming prices of \$25 a barrel, the OECD forecasts a surplus of 15% of GDP this year and next. However, Norway's oil wealth complicates the management of its economy. The government is loosening fiscal policy after the budget surplus reached 14% of GDP last year. But falling financial markets have cut the value of Norway's overseas investments and somewhat reduced the government's room for manoeuvre. Although the oil-related rise in the krone has hurt competitiveness, GDP growth on Norway's mainland is expected to rise to 1¼% this year and 2½% in 2003. With the economy near capacity, looser fiscal policy means that monetary policy has to be tight. Interest rates were raised in July by a half-point to 7%. By pushing the krone up, high oil prices may obviate the need for more rate rises.

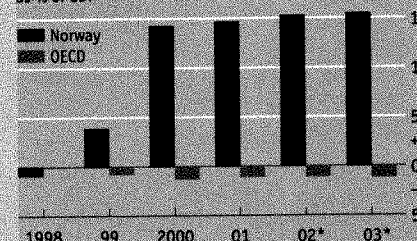
GDP

% increase on a year earlier



Current-account balance

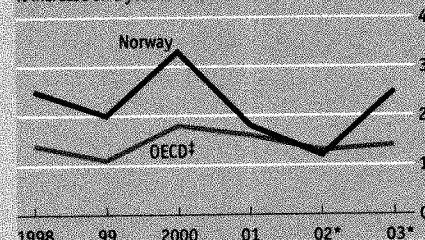
as % of GDP



Source: OECD

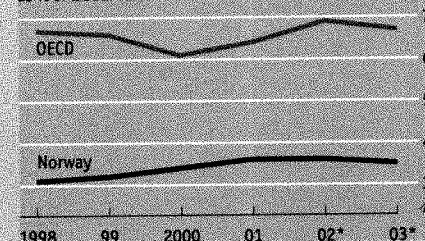
Consumer prices†

% increase on a year earlier



Unemployment

as % of labour force



*Forecast †Private-consumption deflator ‡Excluding Hungary, Mexico, Poland and Turkey

Money and interest rates

	Money supply*			Interest rates % p.a. (Sep 11th 2002)					
	% change on year ago			3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds
	narrow	broad		latest	year ago		latest	year ago	
Australia	- 4.1	+ 9.4	Jul	4.91	4.42	5.01	5.58	5.45	6.58
Britain	+ 8.6	+ 5.7	Jul	3.94	4.75	3.93	4.56	4.83	5.77
Canada	+17.2	+ 7.2	Jul	2.82	3.55	3.39	4.97	5.20	6.79
Denmark	+ 6.2	+10.2	Jul	3.40	4.61	3.84	4.72	5.07	6.85
Japan	+31.5	+ 3.5	Aug	0.02	0.01	-0.02	1.04	1.39	1.15
Sweden	+ 2.2	+ 4.2	Jun	4.20	4.35	4.48	5.02	5.14	5.03
Switzerland	+10.9	+ 5.8	Jul	0.75	3.01	0.70	2.75	3.22	3.85
United States	+ 5.2	+ 7.4	Jul	1.73	3.24	2.19	4.06	4.73	6.32
Euro area†	+ 7.6	+ 7.1	Jul	3.32	4.18	3.39	4.47	4.76	5.35

* Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 4.88%, Japan No.241 1.05%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.001%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Stockmarkets

Market indices

	Sep 11th	2002		% change on		
		high	low	one week	record high	Dec 31st 2001 in local currency in \$ terms
Australia (All Ordinaries)	3,097.6	3,440.0	2,937.8	+ 1.6	-10.0	- 7.8 - 1.4
Austria (ATX)	1,131.9	1,357.2	1,109.5	+ 0.7	-34.8	- 0.7 + 8.3
Belgium (Bel 20)	2,260.8	2,899.8	2,001.6	+ 4.8	-38.6	-18.7 -11.3
Britain (FTSE 100)	4,210.7	5,323.8	3,777.1	+ 4.6	-39.2	-19.3 -14.2
Canada (Toronto Composite)	6,618.3	7,958.1	6,161.1	+ 1.5	-41.9	-13.9 -12.8
Denmark (KBX)	187.0	233.4	169.0	+ 2.7	-38.0	-16.8 - 9.1
France (SBF 250)	2,272.1	3,081.9	2,067.7	+ 5.8	-48.3	-23.8 -16.8
(CAC 40)	3,397.0	4,688.0	3,023.7	+ 7.2	-50.9	-26.5 -19.8
Germany (Xetra DAX)	3,584.7	5,462.6	3,332.7	+ 4.6	-55.6	-30.5 -24.2
Italy (BCI)	1,173.2	1,513.0	1,077.8	+ 3.4	-46.2	-18.1 -10.7
Japan (Nikkei 225)	9,400.1	11,979.9	9,075.1	+ 3.6	-75.8	-10.8 - 3.1
(Topix)	917.1	1,139.4	886.4	+ 3.5	-68.2	-11.1 - 3.4
Netherlands (AEX)	367.4	531.2	318.5	+ 5.0	-47.6	-27.5 -20.9
Spain (Madrid SE)	675.0	848.1	625.9	+ 4.7	-41.1	-18.1 -10.6
Sweden (Affarsvarlden Gen)	154.0	236.8	143.1	+ 4.3	-61.5	-33.4 -25.8
Switzerland (Swiss Market)	5,250.9	6,694.1	4,607.8	+ 5.9	-37.6	-18.2 - 9.8
United States (DJIA)	8,581.2	10,635.3	7,702.3	+ 1.9	-26.8	-14.4 -14.4
(S&P 500)	909.5	1,172.5	797.7	+ 1.8	-40.5	-20.8 -20.8
(Nasdaq Comp)	1,315.5	2,059.4	1,206.0	+ 1.8	-73.9	-32.6 -32.6
Europe (FTSE Eurotop 300)*	958.3	1,279.7	862.3	+ 5.8	-43.8	-24.0 -17.0
Euro area (FTSE Ebloc 100)*	809.5	1,125.1	732.5	+ 6.6	-47.8	-27.2 -20.5
World (MSCI)†	821.6	1,024.4	756.7	+ 2.2	-43.3	na -18.1
World bond market (Salomon)‡	493.8	504.2	430.3	- 1.7	- 2.1	na +12.3

* In euro terms. † Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡ Salomon Smith Barney World Government Bond Index, total return, in \$ terms.

The Economist commodity price index

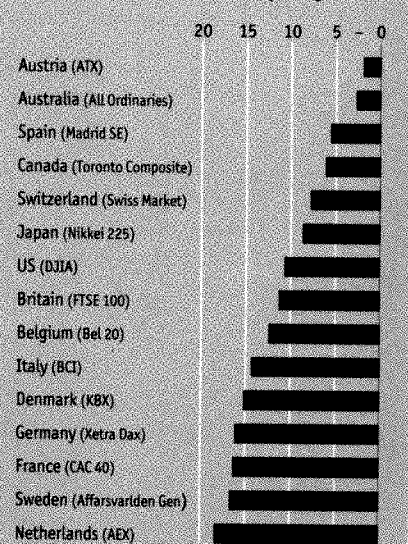
1995=100

	Sep 3rd	Sep 10th*	% change on one month	% change on one year
Dollar index				
All items	73.8	76.4	+ 4.0	+14.5
Food	78.3	81.9	+ 5.4	+20.8
Industrials				
All	67.7	68.8	+ 1.8	+ 5.7
Nfa†	70.5	70.9	- 0.2	+ 8.0
Metals	65.3	67.1	+ 3.7	+ 3.7
Sterling index				
All items	74.4	77.6	+ 2.6	+ 8.4
Euro index				
All items	97.4	103.1	+ 4.4	+ 6.7
Yen index				
All items	92.0	97.3	+ 4.5	+15.6
Gold				
\$ per oz	313.95	318.20	+ 1.0	+10.3
West Texas Intermediate				
\$ per barrel	27.77	29.64	+ 6.0	+ 7.3

* Provisional. † Non-food agriculturals.

Stockmarkets

September 11th 2002, % fall on a year ago



Trade, exchange rates and budgets

Trade balance*, \$bn latest 12 months			Current account				Exchange rate		Currency units					Budget balance % of GDP 2002†
			\$bn latest 12 mths	The Economist poll % of GDP, forecast 2002 2003			trade-weighted‡ Sep 11th	year ago	per \$ Sep 11th	year ago	per £	per euro	per ¥100	
Australia	- 1.3	Jul	- 11.6	Q2	- 3.7	- 3.8	73.4	71.3	1.83	1.93	2.83	1.78	1.52	0.1
Austria	- 2.0	May	- 1.3	Jun	- 2.2	- 1.9	na	100.3	1.03	1.10	1.59	-	0.85	-0.3
Belgium	+ 15.1	Jun	+ 11.8	Mar§	+ 5.0	+ 5.1	na	99.0	1.03	1.10	1.59	-	0.85	nil
Britain	- 44.9	Jul	- 31.2	Q1	- 2.1	- 1.9	106.6	106.6	0.65	0.68	-	0.63	0.54	-0.8
Canada	+ 34.0	Jun	+ 12.1	Q2	+ 2.1	+ 2.2	75.5	76.9	1.58	1.56	2.44	1.53	1.31	1.0
Denmark	+ 7.2	Jun	+ 3.5	Jun	+ 1.9	+ 1.8	102.8	102.6	7.64	8.22	11.8	7.42	6.34	2.2
France	+ 9.0	Jun	+ 28.4	Jun	+ 1.7	+ 1.6	na	101.7	1.03	1.10	1.59	-	0.85	-2.0
Germany	+104.5	Jul	+ 30.2	Jul	+ 1.2	+ 1.0	na	98.7	1.03	1.10	1.59	-	0.85	-2.8
Italy	+ 9.8	Jun	- 2.9	May	- 0.1	- 0.0	na	72.6	1.03	1.10	1.59	-	0.85	-1.4
Japan	+ 83.8	Jul	+110.9	Jul	+ 2.9	+ 2.9	134.9	140.4	121	119	187	117	-	-8.0
Netherlands	+ 23.7	Jun	+ 2.7	Q2	+ 3.9	+ 4.0	na	98.0	1.03	1.10	1.59	-	0.85	0.1
Spain	- 36.4	Jun	- 16.5	May	- 2.1	- 1.8	na	74.2	1.03	1.10	1.59	-	0.85	-0.3
Sweden	+ 14.7	Jul	+ 8.1	Jul	+ 3.2	+ 3.2	77.1	73.0	9.41	10.6	14.6	9.15	7.81	2.1
Switzerland	+ 3.0	Jul	+ 25.7	Q1	+10.0	+10.2	114.1	109.7	1.51	1.66	2.33	1.46	1.25	na
United States	-435.5	Jun	-398.1	Q1	- 4.5	- 4.1	114.4	117.5	-	-	1.55	0.97	0.83	-1.0
Euro area	+ 79.2	Jun	+ 24.8	Jun	+ 0.5	+ 0.5	81.1	78.9	1.03	1.10	1.59	-	0.85	-1.5

* Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. † 1990=100, Bank of England. ‡ OECD forecast. § New series.

Overview

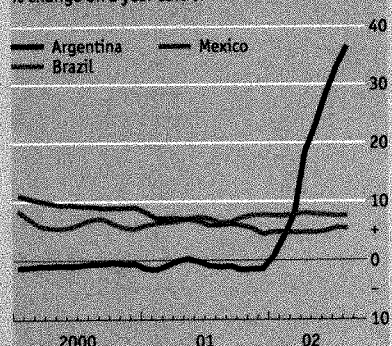
Industrial production rose sharply in several countries in the year to July. In the Czech Republic, it jumped by 10.8%, the biggest rise for 15 months. Output also rose by 12.3% in Turkey and by 7.8% in South Africa. The increase of 6.9% in Malaysia was the fastest for 18 months.

Stockmarkets in Russia and Eastern Europe regained ground. Moscow rose by 3.8% over the week, Warsaw by 4.3%. Asian stockmarkets were more unsettled. Manila rose by 3.5% and Bangkok by 2.7%, but Shanghai and Kuala Lumpur each fell by 2.6%.

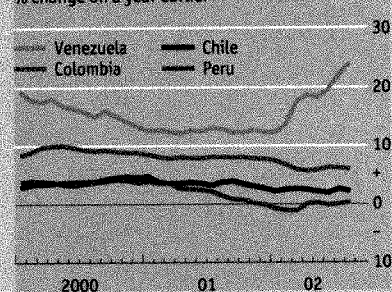
Consumer prices

Argentina has a long history of battling against high inflation. But in the decade to December 2001 it succeeded in achieving price stability by pegging its peso to the dollar, backed by a strict currency-board regime. The recent financial crisis has, however, changed all that. Since Argentina abandoned its currency board in January the peso has fallen by 73%. As the chart shows, inflation has duly shot up. Consumer prices in August were 37% higher than a year ago. Venezuela has the second-highest inflation rate among Latin America's bigger economies. Consumer-price inflation there has doubled over the past year, to 24% in August. At the other extreme, Peru and Chile have inflation rates of only 0.3% and 2.2%, respectively.

% change on a year earlier



% change on a year earlier



Source: National statistics

Economy

	% change on year ago			Latest 12 months, \$bn		Foreign reserves* \$bn, latest
	GDP	Industrial production	Consumer prices	Trade balance	Current account	
China	+ 8.0 Q2	+12.7 Aug	- 0.9 Jul	+28.3 Jul	+17.4 2001	246.8 Jun
Hong Kong	+ 0.5 Q2	-11.6 Q1	- 3.4 Jul	- 8.2 Jul	+14.1 Q1	112.3 Aug
India	+ 6.4 Q1	+ 4.0 Jun	+ 3.9 Jul	- 5.1 Jul	+ 1.4 Q1	58.3 Aug
Indonesia	+ 3.5 Q2	- 9.4 Q4	+10.6 Aug	+27.3 Jul	+ 6.1 Q1	29.5 Jul
Malaysia	+ 3.8 Q2	+ 6.9 Jul	+ 2.1 Jul	+13.4 Jul	+ 7.0 Q1	32.8 Jul
Philippines	+ 4.5 Q2	+ 5.9 Jun	+ 2.9 Aug	+ 2.6 Jun	+ 6.2 May	13.4 Aug
Singapore	+ 3.9 Q2	+17.8 Jul	- 0.4 Jul	+ 6.4 Jul	+17.5 Q2	80.9 Aug
South Korea	+ 6.3 Q2	+ 8.9 Jul	+ 2.4 Aug	+ 9.8 Aug	+ 5.3 Jul	115.4 Jul
Taiwan	+ 3.0 Q2	+11.4 Jul	- 0.3 Aug	+18.6 Aug	+24.8 Q2	155.3 Jul
Thailand	+ 3.9 Q1	+ 9.6 Jul	+ 0.3 Aug	+ 3.8 Jul	+ 6.5 Jul	37.0 Jul
Argentina	-16.3 Q1	-11.2 Jul	+36.5 Aug	+13.4 Jul	nil Q1	9.0 Jul
Brazil	+ 1.0 Q2	+ 3.3 Jul	+ 7.5 Aug	+ 7.4 Aug	-16.7 Jul	39.1 Jul
Chile	+ 1.7 Q2	+ 8.6 Jul	+ 2.2 Aug	+ 2.7 Jul	- 0.6 Q2	15.0 Jul
Colombia	+ 2.2 Q2	- 1.2 Jun	+ 6.0 Aug	+ 0.5 Jun	- 1.4 Q1	10.6 Jul
Mexico	+ 2.1 Q2	+ 1.9 Jul	+ 5.3 Aug	- 9.1 Jul	-16.3 Q2	46.1 Jul
Peru	+ 3.8 Jul	+ 6.8 Jul	+ 0.1 Aug	+ 0.2 Jun	- 1.0 Q2	9.2 Jul
Venezuela	- 9.9 Q2	-17.1 Jun	+24.0 Aug	+ 8.5 Q2	+ 1.9 Q2	7.6 Jun
Egypt	+ 4.9 2001†	+ 7.8 2001†	+ 2.7 Jun	- 8.2 Apr	- 0.1 Q1	12.6 May
Israel	- 1.7 Q2	+ 1.6 Jun	+ 6.9 Jul	- 6.3 Jul	- 2.3 Q1	24.5 Aug
South Africa	+ 2.2 Q2	+ 7.8 Jul	+10.6 Jul	+ 3.1 Jul	- 0.1 Q1	6.0 Jul
Turkey	+ 2.3 Q1	+12.3 Jul	+40.2 Aug	-10.3 Jun	+ 2.0 Jun	23.2 Jul
Czech Republic	+ 2.5 Q2	+10.8 Jul	+ 0.6 Aug	- 2.5 Jun	- 2.3 Q2	21.6 Aug
Hungary	+ 3.1 Q2	+ 5.1 Jul	+ 4.5 Aug	- 2.4 Jul	- 2.1 Jul	10.3 Jul
Poland	+ 0.5 Q1	+ 6.0 Jul	+ 1.3 Jul	-10.4 Jul	- 6.4 Jul	27.1 Jul
Russia	+ 3.7 Q1	+ 7.8 Jul	+15.2 Aug	+42.4 Jul	+28.3 Q2	40.6 Aug

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Financial markets

	Currency units		Interest rates short-term % p.a.	Stockmarkets Sep 11th	% change on		
	per \$ Sep 11th	per £ year ago			one week	in local currency	in \$ terms
China	8.28	8.28	12.8	na	1,691.0	-2.6	- 1.3
Hong Kong	7.80	7.80	12.1	1.77	9,882.4	+0.6	- 13.3
India	48.4	47.4	75.0	5.68	3,125.7	-1.5	- 4.2
Indonesia	8,893	9,040	13,765	14.67	430.1	+2.3	+ 9.7
Malaysia	3.80	3.80	5.88	3.20	689.7	-2.6	- 0.9
Philippines	52.0	51.2	80.4	6.88	1,153.4	+3.5	- 1.3
Singapore	1.76	1.74	2.72	1.06	1,448.5	-0.6	- 10.8
South Korea	1,205	1,285	1,865	4.80	724.7	+0.2	+ 4.5
Taiwan	34.3	34.5	53.1	2.10	4,660.5	+2.8	- 16.0
Thailand	42.5	44.4	65.8	2.00	361.4	+2.7	+ 18.9
Argentina	3.61	1.00	5.59	47.80	386.1	+3.3	+ 30.7
Brazil	3.10	2.67	4.80	17.89	10,182.2	+1.9	- 25.0
Chile	721	682	1,116	2.52	4,905.8	nil	- 9.1
Colombia	2,723	2,343	4,214	7.94	1,202.2	+0.9	+ 12.3
Mexico	9.97	9.46	15.4	6.87	6,260.6	+2.4	- 1.8
Peru	3.61	3.49	5.59	4.27	1,183.5	-0.2	+ 0.7
Venezuela	1,492	746	2,309	20.00	7,195.5	+5.3	+ 9.5
Egypt	4.60	4.26	7.12	7.14	5,241.9	+0.2	- 0.6
Israel	4.75	4.32	7.35	6.40	362.7	+1.5	- 18.8
South Africa	10.6	8.62	16.4	12.65	9,941.5	+4.7	- 4.8
Turkey	1,664,500	1,447,500	2,576,313	42.00	9,268.5	-2.1	- 32.8
Czech Republic	30.6	37.7	47.4	3.02	453.7	+3.2	+ 15.0
Hungary	250	284	387	9.70	7,631.2	+4.0	+ 7.0
Poland	4.16	4.24	6.45	8.15	13,407.0	+4.3	- 3.7
Russia	31.7	29.5	49.0	21.00	346.9†	+3.8	+ 38.5
EMF (MSCI)*	1.00	1.00	1.55	na	297.6	+2.2	na
EMBI+†	1.00	1.00	1.55	na	208.2	+0.7	na

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In \$ terms.

Sources: National statistics offices; central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; UBS Warburg; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; Russian Economic Trends.

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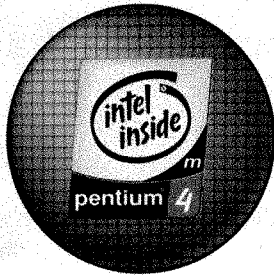
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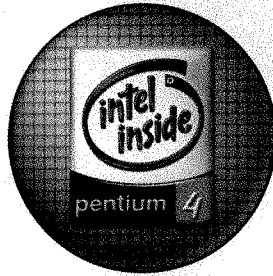
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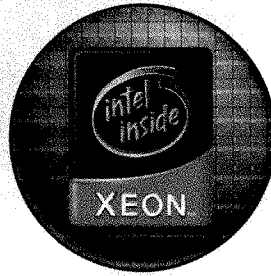
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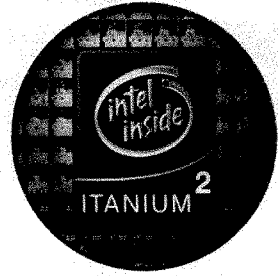
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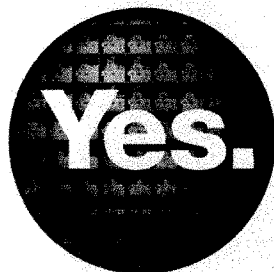


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The Japanese prime minister's historic visit to Pyongyang shows that dealing with North Korea may be getting interesting, but no easier: leader, page 11. He may yet pay a price at home for his trip, page 25

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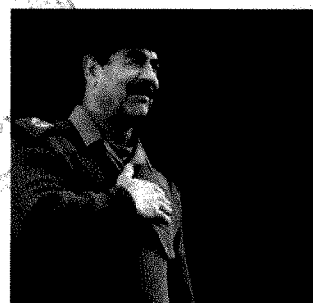
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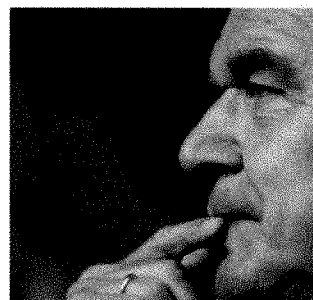
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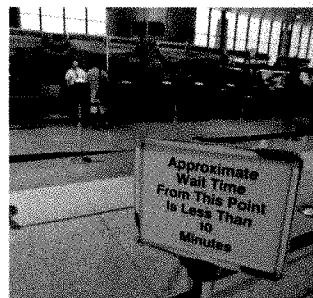
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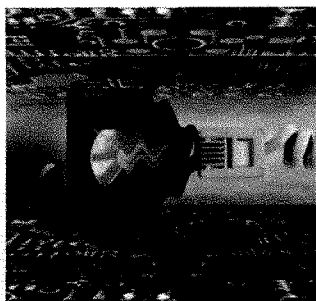
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Politics

In response to American threats, and tough pressure from its fellow Arabs, **Iraq** said the UN's weapons inspectors could return to Iraq, without conditions. Talks between Iraq and the UN began immediately. The United States, expressing scorn for the offer, said it would press for a new Security Council resolution. Some other countries said there was no need.



Ramzi bin al-Shibh, one of **al-Qaeda's** leaders, was arrested in Pakistan and flown to the United States. The FBI also arrested half a dozen alleged members of an al-Qaeda cell in Lackawanna, a steel town in New York state.

Janet Reno finally conceded the Democratic nomination for governor in **Florida** to Bill McBride, after a week of delay due to complaints about voting procedures. Meanwhile, in **Massachusetts** Shannon O'Brien won the Democratic gubernatorial primary; she now faces the Republican candidate, Mitt Romney.

Persson in charge
Sweden's ruling Social Democrats, led by the prime minister, Goran Persson, easily won a general election, scoring nearly 40% of the votes against 15% for the main right-wing party, the Moderates. The populist Liberals took third place, tripling their vote to 13%, partly thanks to a controversial suggestion that immigrants should pass a Swedish-language test.

Ahead of **Germany's** general election on September 22nd, polls put the Social Demo-

crats, led by the chancellor, Gerhard Schröder, just in front of his main conservative challengers, led by Edmund Stoiber, but the shape of a new government may depend on the performance of three smaller parties.

After a general election in strife-ridden **Macedonia**, a coalition of moderate Slavs and the more nationalistic of the two main ethnic Albanian parties prepared to replace a government led by the more nationalist Slav party.

The **Georgian** government, under threat of military action from Russia, insisted that Russians and Americans were already co-operating to pacify the lawless Pankisi Gorge, in the northern part of the country abutting Chechnya, and root out rebel Chechens using the territory for refuge.

French police nabbed two top leaders of the **Basque** separatist terror group, ETA, in a suburb of Bordeaux. The Spanish government hailed the arrests as a blow against terrorism.

The **Irish** government suffered the embarrassment of having to drop a controversial but longstanding plan, known informally as the "Bertie Bowl" after the prime minister, Bertie Ahern, to build a stadium on the edge of Dublin.

Lula edges ahead
Brazil's currency and its bonds slipped again, as Luiz Inacio Lula da Silva, the left-wing front-runner for next month's presidential election, increased his lead in the opinion polls over Jose Serra, the government candidate.

Trade unions in **Colombia** held a one-day strike against public-spending cuts and labour and pensions reforms planned by the new government of President Alvaro Uribe.

Cuba said that it would sign the Nuclear Non-Proliferation Treaty and ratify the Treaty of Tlatelolco, under which the countries of Latin America

and the Caribbean have renounced nuclear weapons.



Dozens of people were injured when police broke up a demonstration by several thousand protesters calling for the resignation of **Paraguay's** president, Luis Gonzalez Machi. Further protests are planned.

The right road?

The so-called **quartet** (America, Russia, the EU and the UN) which is exploring possible solutions to the Palestinian-Israeli conflict offered a three-phase "road map": Palestinian reform and elections, plus Israel's withdrawal to positions it held two years ago; the creation of a "provisional" Palestinian state; and Israeli-Palestinian talks leading to a final agreement in 2005.

Suicide bombers struck twice at **Israel**: first in northern Israel, killing a policeman; second in Tel Aviv, killing at least five people and wounding many more.

Corruption costs Africa almost \$150 billion a year, according to a report from the African Union. This figure, which includes direct costs (money stolen or extorted) and indirect ones (investment scared off), is about 25% of Africa's GDP.

Rwanda started pulling some of its troops out of eastern Congo, as part of a peace pact signed with Congo's government in July.

Nigeria's electoral commission suspended voter registration in parts of four states where ethnic and religious fighting had made it difficult. A commission reported that riots in one of the states last

year had killed 915 people—twice previous estimates.

Hundreds of laid-off soldiers started shooting in Abidjan, the capital of **Côte d'Ivoire**, before dawn on September 19th. The government denied that it was an attempted coup, and said the situation was under control.

Bullets and ballots

Election violence continued in Indian-administered **Kashmir** as Islamic militants killed two ruling-party activists in Srinagar. But Indian officials said that turnout for the start of voting, which takes place in stages until October, was high.



The ground-breaking visit by Japan's prime minister, Junichiro Koizumi, to **North Korea** prompted an apology from Kim Jong Il, the North Korean leader, for the abduction of 12 Japanese civilians during the 1970s and 1980s. Japan had demanded answers over its missing citizens as a pre-condition for talks on normalising relations between the two countries.

After historic talks in Thailand between **Sri Lankan** officials and the separatist Tamil Tigers, Anton Balasingham, a rebel negotiator, clarified his group's long-term aim by stating that they would settle for autonomy for minority Tamils rather than a separate state.

Afghan authorities arrested a senior Taliban official and three of his aides in the southern province of Kandahar. All four were handed over to American forces in the city.

At least 38 people died in a mass poisoning near Nanjing in **China**. Police blame a rival shopkeeper.

Business

The trust controlling **Hershey Foods** decided not to share its sweets. Caving in to political pressure and public outcry centred on the company town in Pennsylvania, it abandoned plans to auction Hershey, America's biggest confectioner, for around \$12 billion.

Investment Bank

The **Bank of Japan** stunned the markets by announcing that it planned to prop up the country's ailing banks by buying shares directly from them in a bid to stabilise the financial system. The dwindling value of Japan's stockmarket has reduced the banks' capital as they struggle to write off their vast bad debts. Observers wondered how close to disaster the banks really are.

Lukas Mühlemann agreed to step down as chairman and chief executive of **Credit Suisse** in December, so deciding the succession at the top of the Swiss bank. Walter Keilholz, head of Swiss Re, will become chairman; Oswald Grübel and John Mack will slug it out as joint CEOs.

Shares in **J.P. Morgan Chase** plunged by 5% after the American investment bank gave warning that bad loans to telecoms companies and falling trading revenues would dent its third-quarter profits.

Asbestos pay-outs hit another European insurer. **Allianz**, a German giant, was forced to give \$750m to an American unit to cover asbestos-related claims. Its shares sagged as investors feared that it will join the queue of insurers proffering a begging bowl to secure fresh capital. Swiss Life was the latest to hold out its hand after announcing a first-half loss of SFr386m (\$236)—it wants SFr1.2 billion.

The woes of Europe's insurers and general worries about the state of the world economy hit **European stockmarkets**. The FTSE 100 fell by 4% in one day, Germany's DAX fell by 5% to a

five-and-a-half-year low. Other markets followed suit.

OPEC agreed to keep tight production quotas despite winter and a war in Iraq looming. Oil prices seem likely to rise.

Executive perking

Dennis Kozlowski, a former CEO of Tyco International, and two other top executives were charged with fraud. Its alleged extent? Unauthorised payments to employees of nearly \$100m. Mr Kozlowski is also said to have improperly spent company funds on personal luxuries including a dog umbrella stand costing \$15,000, \$2,900-worth of coat-hangers and a notebook at a more modest \$1,650.

America's Securities and Exchange Commission began an "informal investigation" into **General Electric's** accounting treatment of a generous retirement package awarded to Jack Welch, even though the company's former boss agreed to forgo many of the benefits to protect GE's reputation.

The mood of accounting rectitude sweeping America failed to overwhelm Silicon Valley. A distinguished commission made up of business grandees endorsed the costing of **stock**

options on company books—save one man. Andrew Grove of Intel, the chip-making behemoth, spoke for many among America's tech elite, saying that the move will merely punish firms that distribute options widely—ie, the inhabitants of Silicon Valley.

Phone votes

MobilCom had the good fortune to face bankruptcy a week before Germany's general elections. Gerhard Schröder, chancellor for the time being, announced a vote-courting bail-out to the tune of some €400m (\$391m) for the beleaguered mobile-phone operator. It was still said to have plans to axe a third of its staff of 5,500, which could prompt the government to withdraw the lifeline.

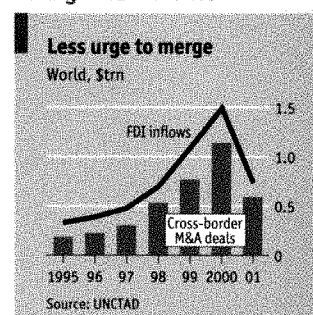
Deutsche Telekom may profit from the ills of Elektrim, a Polish company that owns 51% of the country's leading mobile firm (with Vivendi Universal). DT's 49% stake may allow it to snap up the rest at a knock-down price

Harvey Nichols, an upmarket British designer-goods store much favoured by "ladies who lunch", is to return to private hands. Dickson Poon, the shop's owner, offered to

buy back a 49.9% stake for a less than luxurious £2.50 (\$3.80) a share, a little less than the offer price in 1996.

Scientists at CERN, a particle-physics laboratory in Switzerland, announced the creation of 50,000 anti-hydrogen atoms. It is the first time that **atomic anti-matter** has been made in such bulk. Not quite enough to power the starship *Enterprise*, though.

Foreign indifference



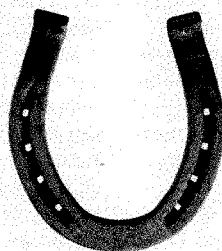
Foreign direct investment fell by 51% in 2001 to around \$735m, the biggest decline for over 30 years according to the *World Investment Report*. Despite the sudden waning of the cross-border merger frenzy, America still remains the biggest recipient of FDI with inflows of \$124 billion.

Other economic data and news can be found on pages 96-98

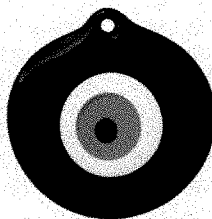




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The apologetic kidnapper

Dealing with North Korea may be getting interesting, but no easier



AHANDSHAKE and a pair of Apologies are a start. But will this week's controversial trip to Pyongyang by Japan's prime minister, Junichiro Koizumi, help reshape the history of confrontation between North Korea and the outside world, or

merely offer another footnote to disappointment?

Much depends on what North Korea's leader, Kim Jong Il, is up to: is he genuinely searching for a way out of his bunker, or merely looking for a fresh pocket to tap for the funds he needs to survive? Quite possibly, both. But even assuming that he is ready to start settling at least some of his long-standing differences, not just with Japan, but also with South Korea and the United States, peace on the Korean peninsula can best be won if these three countries stick together as closely in their dealings with the unpredictable Mr Kim in the future as they have in the recent and difficult past.

Mr Koizumi did not return empty-handed from this first ever Japan-North Korea summit. He brought back news of some Japanese citizens who had been kidnapped over the years by North Korean agents, and he won a pocketful of promises (see page 25). Mr Kim said he would resume stalled talks about normalising relations with Japan, drop demands for "reparations" for Japan's past colonial rule in favour of "economic aid", extend his moratorium on missile testing beyond the turn of the year, and keep to his obligations under a 1994 nuclear deal brokered by America that traded a halt to North Korea's production of bomb-usable plutonium for two western-designed nuclear reactors now being built.

All that is probably as much as Mr Koizumi could have expected—perhaps more, since in return for Japan's (previously proffered) apology for its past colonial behaviour, Mr Kim not only said he was sorry for the kidnappings, but promised not to reoffend. After years of bare-faced denials, such bare-faced contrition seemed something of a breakthrough. Yet it is also a measure of how difficult it will still be for Japan, South Korea and the United States to reduce the threat to regional stability from a regime that has so far made a national virtue out of remaining the last, dangerous relic of the cold war in Asia.

Aside from his hopes of a lift in the opinion polls at home, Mr Koizumi's chief aim this week seemed to be to show that, for all its economic woes, Japan was still a player in resolving the region's security problems. His officials point to Mr Kim's promise to hold off from further missile tests, and his readiness to live up to North Korea's commitments under the 1994 nuclear deal, as evidence of success. But North Korea has promised all these things before. Is there reason to believe they may add up to something this time?

He may run North Korea with an iron rod, but Mr Kim is not entirely immune to domestic pressures. In recent years, famine has killed some 2m North Koreans (out of about 22m), and only foreign food aid has saved many of the rest. But floods and drought have merely compounded a man-made disaster brought on by decades of Stalinism. Alarmed by the increas-

ing outflow across its border of desperate North Koreans, China has long been pressing Mr Kim to change his ways. A revamp of wages and prices two months ago appears to be his attempt to imitate China's Communists, by reviving the economy while keeping a firm grip on power. With Russia and South Korea, Mr Kim has dusted off plans for a rail link that could eventually carry freight all the way to Europe.

But, as China no doubt reminds him, Mr Kim cannot find the huge sums he needs to rebuild his country's broken infrastructure without help from South Korea, Japan and America. He has tried South Korea: two years ago a summit in Pyongyang with South Korea's president, Kim Dae-jung, ended with promises of large dollops of South Korean aid in return for greater contact across the inter-Korean divide. But the northern Mr Kim kept up the hostility, while pocketing what cash he could. He then tried auctioning off his missile programme to the Clinton administration, which was anxious to see an end to North Korea's proliferation activities in unstable parts of the world, such as South Asia and the Middle East. But the deal was unfinished when George Bush decided to put an end to the practice of buying off North Korea's bad behaviour, since this seemed only to encourage more of it.

Keeping his attention

For more than a year now, Mr Bush has been offering North Korea an across-the-board improvement in relations, but only if North Korea starts attending just as comprehensively to the security threat it poses. This would mean not just ending its missile programme, but also admitting international inspectors to check on its past plutonium dabbling, as North Korea is obliged to do before the nuclear components for its new reactors are delivered. It would also mean discussing confidence-building measures to reduce the threat to South Korea from North Korean troops and artillery massed across the border.

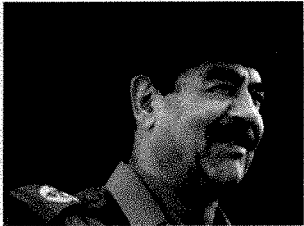
Mr Kim, miffed at being included in George Bush's "axis of evil", had seemed to turn that offer down flat. But it's a funny thing. Ever since Mr Bush declared his war on terrorism and weapons of mass destruction, Mr Kim has moved, despite the occasional zig-zag, in roughly the right direction: he has signed a series of UN conventions outlawing terrorism; he has moved to start expelling some ageing Japanese terrorists he had been harbouring; and now he has owned up to snatching those Japanese citizens, and sent Mr Koizumi home with a message that he is ready for talks with others, America included.

And not before time. Unless the inspection issue can be resolved soon, the reactor project could start to unravel, pitching the peninsula back towards confrontation and leaving North Korea with no check on its nefarious nuclear activities. Mr Kim had clearly been hoping that South Korea would provide an alternative source of the electricity the reactors are meant to provide, but it has so far refused. If Japan's promised aid flows too quickly, that might be another way he tries to wriggle off the inspections hook. Letting him do that would be sheer folly. Only by standing together and standing firm have America, South Korea and Japan coaxed Mr Kim this far out of his bunker. There is still a lot of careful coaxing to do. ■

Iraq and the UN

Saddam under pressure

Keep him that way



THE past week has been good for President George Bush and bad for President Saddam Hussein. Mr Bush's stirring and well-crafted speech to the United Nations General Assembly on September 12th convinced many other countries, most notably other permanent members of the Security Council, to support the idea of new resolutions laying down the world's demands on Iraq. Arab countries that had been widely assumed to oppose a war on Iraq in almost any circumstances suddenly changed their minds, saying that, well, if the UN were to be behind a war then yes, of course American and other forces could use bases on their territory. Given all that, it is hardly surprising that Mr Hussein then performed a somersault, dropping his previous absolute rejection of any idea that UN weapons inspectors should return to his country after their four-year exclusion, and sending a short letter saying that inspectors could return after all. Even dangerous dictators have survival instincts.

What has been surprising—or, rather, dispiriting—has been the reaction to Mr Hussein's somersault by many western commentators and some western governments. Plainly, the reason why Mr Hussein has changed his mind is that at last, for the first time since the end of the Gulf war in 1991, he faces a credible threat of military attack, supported by the important members of the UN and even by his Arab neighbours. So what, for example, does the foreign minister of Russia say? In effect, that the pressure can now be relaxed, that no new Security Council resolutions are needed, and that all will now be well. The only charitable way to interpret such a position is that it could be a clever feint to tempt Mr Hussein to show his true nature by modifying his offer again in the belief that the world's great powers are disunited once more. More likely, however, Igor Ivanov and others who echo such views are simply being recklessly irresponsible.

Resolute about resolutions

Might Saddam Hussein's offer be sincere? Might he really be willing to readmit the weapons inspectors unconditionally, allow them unimpeded access throughout Iraq, and accept complete disarmament of his chemical, biological and nuclear weapons or facilities? The possibility can be dismissed immediately. For even Mr Hussein will not know whether he is being sincere, at this point. On every single occasion in the past he has not been, for he has always done as little to reveal and disarm as he could get away with. That is natural, for evasion is in his interest. The same will be true now: he will do as little as he can get away with. It is just that he does not yet know how little or how much that will be.

The task for the outside world is to make sure that he has to be sincere, in every single respect. And the only way to do that is to keep up the military and diplomatic pressure. Indeed now would be a fine time to intensify it, given that Mr Hussein has shown in the past few days that he will blink under such

pressure. America's military build-up, through exercises and forward deployments of troops, ships and aircraft should continue, in a steady but remorseless fashion. Iraq's Arab neighbours, especially Saudi Arabia, should keep up their diplomatic arm-twisting, both privately and publicly, to try to persuade Mr Hussein to make further concessions (see page 41). Above all, the Security Council needs to draft and then pass new resolutions about Iraq as soon as possible, setting terms that are as tough as possible.

Some will argue that such resolutions are unnecessary, for all that is needed is for Iraq to fulfil the terms of the previous 16 resolutions laid down for it during the past 11 years. If only they meant it, for most who take this view think that only resolutions about weapons inspectors and disarmament need to be enforced, and not ones about Kuwaiti prisoners-of-war, Kuwaiti property or respect for Iraqis' human rights, among others. Yet two points argue for new resolutions. One is that this was the path the Security Council was heading down after Mr Bush's speech, and so to abandon it now would be to hand an unnecessary victory to Mr Hussein. A display of unchanged determination would put him back on the defensive. The second is that Mr Hussein's successfully evasive record during the 1990s makes it vital to set tougher conditions, using tougher wording and tougher methods, if there is to be any chance of success. In particular, inspectors will need the help of UN troops if they are to be able to do a proper job. At the same time, the demands in a new resolution can and should be set as broadly as is necessary to encompass the subject-matter of all the 16 resolutions he has flouted.

Call his bluff

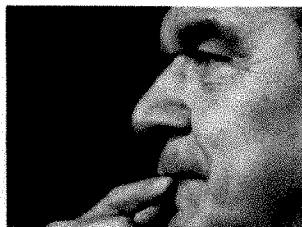
For the United States and Britain to press for such a new resolution, or if necessary two new resolutions, will be risky. There will be a chance that France, Russia and China will withdraw the support or (in China's case) acquiescence they were previously showing. But, having gone so far to rally the UN, that is a risk worth taking. If France and Russia pull back merely because of one offer from a serial liar and murderer, then their support can never have been genuine in the first place. It is more probable, though, that with careful diplomacy and bargaining, they will be persuaded to fall in line.

Their bluff, in other words, will have been called. But the most important bluff to call is that of Saddam Hussein himself. He has long ago forfeited any right to be trusted. He has also forfeited the normal rights of sovereignty by his slaughter of his own people and his violations of international treaties, giving the outside world every right to be thoroughly intrusive in his internal affairs. The hope has to be that the more intrusive outsiders become, the more Mr Hussein's power will be eroded. The dream must be that one day soon he will join Slobodan Milosevic, another brutal dictator, in the dock for crimes against humanity. The worst fear, though, should be that he would succeed again in emulating a much more humorous man with a moustache, Groucho Marx, who said that sincerity was the most important asset in life: if you can fake that, you've got it made. Don't let him. ■

The German election

Time for a change

Gerhard Schröder and his Green allies have disappointed. Germans should risk an alternative



EUROPE'S most powerful country holds an election this weekend whose outcome will be crucial for its ailing economy and for its standing in the world. But even inside Germany you would hardly know it. The economy is seriously, not

just passingly, sick. It has grown more slowly, in the past eight years, than that of any other of the world's rich countries, bar Japan. How odd, then, that this blunt but undeniable diagnosis is not fully accepted by either of the main contenders in the election, Gerhard Schröder, the Social Democratic chancellor, and Edmund Stoiber, his conservative challenger. Both say that Germany needs reform. Who doesn't? But neither has the grit to risk even short-term unpopularity by proposing the necessarily painful treatment to ensure economic revival.

Mr Schröder, moreover, is beset by that enduring weakness of the able tactician, who never quite makes the grade as a statesman: he cannot resist promoting bad policies to earn cheap popularity, especially before elections. Witness, this week, his hectic rush to rescue MobilCom, a failed German telecoms company; and witness, even more plainly, his enthusiasm for rubbishing a possible American-led attack against Iraq, even if it were sanctioned by the United Nations.

What a pity. For if he were judged by his first two-and-half years in office, Mr Schröder would have merited another term (see page 22). For sure, his first year was a muddle. He lost valuable time, and the chance to grab the post-election initiative, as his disruptively ambitious finance minister destroyed himself. But with the opposition pole-axed by a party-finance scandal, Mr Schröder had a fair wind behind him—and began to take advantage of it. He embarked on an impressive series of tax-cutting reforms, made a tentative but worthy effort to persuade people to start buying private pensions, and seemed bent on the sort of liberalisation laid out in a go-ahead document issued jointly with Britain's Tony Blair.

He did the right things in foreign policy too. He broke a post-war taboo by proving ready, without alarming the neighbours, to assert Germany's own interests. He had the laudable nerve to send German troops alongside their allies into war-zones, in the Balkans (and more recently in Afghanistan). He also loosened Germany's old nationality laws, based on blood, and began sensibly liberalising immigration.

He blew it

But then, with the economy growing more perkily again in 2000, the old opportunism seemed to return. With the opposition still adrift, re-election seemed assured. Mr Schröder backed away from tackling the biggest causes of Germany's sluggishness: its over-protected workforce, reluctant to change and expensive to employ, and its strangulating red tape. He recently and belatedly endorsed a clutch of useful proposals by a Volkswagen man, Peter Hartz, to improve job-seeking and job-creating procedures, but the plans still failed to tackle the deeper causes of Germany's labour-market sclerosis. The

global downturn and the burden of Germany's former communist east have made his task no easier. But they are not the main reasons for Mr Schröder's broken promise to bring unemployment to below 3.5m. Over 4m now lack jobs.

As an alternative, Mr Stoiber scarcely sparkles. He looks competent and businesslike. He impresses Germany's small and middling businessmen, whom he rightly sees as the touchstone of Germany's prosperity. He rather airily promises to cut taxes, squeeze debt and the deficit, and bring spending down—all a bit more eagerly than Mr Schröder does, though with no more precision. But Mr Stoiber, too, has meddling instincts, and is unduly wedded to the corporatism and consensus that, though they served Germany well after the war, now seem unable to provide it with pep.

On the social side, he has been at pains to distance himself from the bluff, beer-swilling Bavarian bigotry lampooned by northern cartoonists. But, in contrast to the charming, laddish Mr Schröder, he comes over as narrow, schoolmasterish, a shade intolerant, and lacking in warmth. Mr Stoiber's recent crude banging of the anti-immigration drum has smacked of Mr Schröder's own electoral opportunism.

Schroiber versus Schroiber

Above all, neither man gives the impression that he believes Germany's economy to be truly sick—and therefore in need of the kind of attention that might risk social strife. Perhaps, like the Japanese, many Germans look to their excellent infrastructure, generous welfare and cosy way of life, compare them with the rough-and-tumble of labour law and the frayed public services of, say, Britain and the United States, and think, well, why worry? Perhaps slipping down a rung or two in international league tables of wealth and growth is a price worth paying for serenity and social cohesion. The trouble, of course, is that the slippage can accelerate—and all those comforts may, sooner rather than later, be menaced too.

Despite his cautious conservatism, Mr Stoiber is more likely to listen to those who preach the need for the sort of economic medicine that might court some unpopularity. And in foreign policy, he has some shrewd advisers. They would surely have prevented a German chancellor from endangering relations with the United States even if he had wanted to counsel against an attack on Iraq.

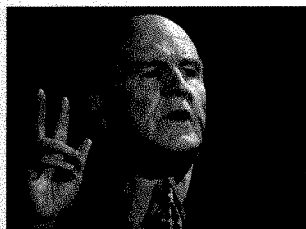
Much will depend, if the election is as close as predicted, on the small parties—the Free Democrats (or liberals), the Greens and the ex-communists. A grand coalition of the two big parties is sometimes mooted. But that could well be a recipe for consensus-bound fudge. The only party in Germany that has consistently proposed ways to tackle the roots of the malaise is the liberal FDP. It alone argues for a wholesale unshackling of Germany's hidebound, suffocating economy.

The most hopeful outcome would be a coalition of Mr Stoiber's lot with a robust contingent of liberals yapping at his side. The deeper problem, however, is that too few Germans seem ready for a wrenching change. It may take another four years of steady decline before they realise just how badly they are going to need it. ■

Chief executives

Easing the pain of parting

How to say goodbye to the boss



JANE WELCH has done General Electric's shareholders a favour. By listing in an affidavit as part of her divorce proceedings the cornucopia of benefits that her husband was offered by his generous colleagues on his retirement, she revealed what

had not been fully disclosed to shareholders or the Securities and Exchange Commission (SEC): the country-club fees and corporate jets, flowers and groceries, help with the \$80,000 a month Manhattan apartment and financial-planning services (although, with a deal like that, who needs them?).

It is amazing what a little transparency can do. Faced with what he described as "a helluva problem"—of deciding whether to alter the contractual agreement to shower him with such bounty—Mrs Welch's husband Jack has done the decent thing. He has decided to turn at least some of it away (see page 63) and restore the reputation he gained in the 1990s as an executive hero when he headed GE.

At least Mr Welch appears to have left GE in good shape, and built value for its shareholders. Many other bosses do far worse—and still expect a reward. Take that egregious example, Linda Wachner of Warnaco, claiming a vast pay-off from her bust business. Bosses from Jean-Marie Messier at Vivendi to Percy Barnevik at ABB, a Swiss engineering giant, seem to find greed hard to resist even when they are leaving a fallen star. How should responsible companies say goodbye?

For a start, they should think about that question first when they hire a new boss. In the flush of early excitement, it is all too easy to forget that a relationship may turn sour—and the figures for turnover at the top suggest a steeply rising corporate

divorce rate. In Britain, most chief executives in big firms now have a one-year contract only; in America, the average is three. That swells the payment to a boss forced to leave early.

Then, when the boss eventually goes, the board's compensation committee should grit its teeth and stand firm. A chief executive's departing pay-off should reflect returns that shareholders have enjoyed under his reign. If the company has floundered, then bonus payments should certainly not be part of that pay-off. But, as Jeffrey Sonnenfeld, author of an extensive study of the subject, points out, even successful departing bosses often try to ease the pain of re-entry into normal life by demanding to keep the trappings of their heroic stature: limousines, offices, private jets. Such perks are hard to evaluate and an unreasonable addition to a generous pension.

Next, go for transparency. SEC rules oblige companies to disclose details of the departing boss's contract. But awkward information is squirreled into footnotes, or hidden behind such inscrutable phrases as "in a manner similar to" what the boss enjoyed when he was an employee. Hiding perks in such ways suggests that—well, there is indeed something to hide.

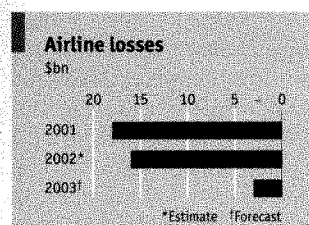
Guard against buried bombs

Finally, companies ought to ensure that a departing chief executive's rewards reflect the continuing success of the company. All too often, an incoming boss finds the place littered with unexploded bombs, planted by his predecessor. In order to discourage such behaviour, some of a departing boss's pay-off could sensibly be tied to future, not past or current, corporate performance. One way is to use restricted stock that cannot be sold for, say, three years. A big award is justified only if it serves a useful purpose—such as persuading bosses to worry about what happens after they leave. ■

Airlines

Grow up

Time for airlines to stand on their own undercarriage



space for four days at enormous cost to the carriers, which were left with aircraft and crews all over the place. A shorter shut-down might have sufficed; certainly the closure of Washington, DC's local airport for weeks did untold damage to US Airways, so ensuring that it was the first of the big network carriers to go into Chapter 11 bankruptcy.

The greatest virtue of the rescue package was that it was

THE \$5 billion compensation that the American government shelled out to airlines immediately after the terrorist attacks in September last year was generous, but understandably so. After all, the government had shut down American air-

done quickly. America, more than any other country, needs a properly functioning airline system. So there is an argument that it is in the public interest to use taxpayers' money in order to put the system back on its feet. But not without limit. The real question is whether the government was wise also to line up another \$10 billion in guaranteed loans through the Air Transportation Stabilisation Board, a body created specially for the purpose. It might have been better, after the initial hand-outs, to have let the airlines sink or swim.

The case for leaving the airlines' fate in the hands of the market becomes stronger as it becomes clearer that the industry's troubles really pre-dated September 11th. In the late 1990s, in both America and Europe, airlines went on blithely increasing capacity and allowing labour costs to balloon even as their core market matured. The result can be seen in the con- ►

▶ tinuing huge losses forecast for this year and next. The only growth is among no-frills carriers, which offer cheap fares for cost-conscious travellers, and threaten the business model of the mainstream airlines (see page 57).

Wider repercussions

One of the unfortunate side-effects of the Americans resorting to subsidies is that it has set a bad example just as the Europeans are trying to kick the habit. This summer Alitalia managed to persuade the European Union to approve yet another national rescue package disguised as a capital increase. Next in line is Olympic Airways, Europe's perpetual flying basket-case, which the Greek government has been talking about privatising for over a decade.

Such bail-outs would not be necessary were airlines not a protected species, with international trade governed by inter-governmental deals and with bans on foreigners taking control. In recent years deals between America and some European countries, such as France and Germany, have become more liberal. But the British-American deal, on the busiest of transatlantic routes between two normally free-trading nations, restricts competition to a cosy club of two British and

two American carriers at crowded Heathrow, the London destination all carriers prefer. Given the impracticality of getting the world's 200-odd international airlines (and the governments that own many of them) to opt for free trade, the best way to liberalise aviation is through regional blocks.

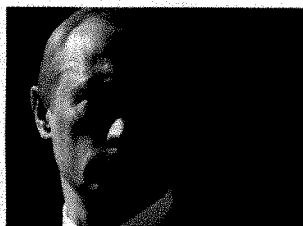
The European Commission, which has successfully followed America in liberalising its internal market, needs to sit down with the Americans to work out an overall "open skies" package that would go much further than existing bilateral deals between individual European countries and the United States. If the two biggest aviation markets in the world could thus link their two liberalised regions in a transatlantic common aviation market, the rest of the world would be under strong pressure to follow their example.

The industry that has done so much to facilitate globalisation would then itself join the process, to the greater good of both shareholders and travellers. Sorting out the problems of over-capacity would become easier as consolidation took place across national borders. Moreover, the sort of benefits that no-frills carriers are bringing to the liberalised American and European markets would become available in some form for long-haul travel too. ■

Russia and Georgia

Putin's folly

Russia would do better to bolster Georgia's stability, not undermine it



THOSE who write speeches for Russia's president, Vladimir Putin, no doubt imagine they are good students of American foreign policy. They seem determined to copy, or rather caricature, every new American idea. They no doubt had a hand,

too, in drafting the stern letter that Mr Putin sent to the United Nations, laying out his case for intervention in neighbouring Georgia unless its government clears its territory of a group of Chechen terrorists who have holed up there.

Like America in Iraq, his officials claim, Russia is insisting on its right to take military action, alone if necessary, against a nation which it deems to be in breach of international law; like America in Afghanistan, Russia justifies itself by recalling that failed states can be a source of festering security threats. Like George Bush, Mr Putin is merely proposing to act pre-emptively, in *extremis*, against a state that poses a deadly and increasing danger. Indeed, regime change cannot be ruled out.

A mixture of all these arguments has been used by Mr Putin and his lieutenants to justify their recent and repeated threats of military action against Georgia—some air raids have already taken place, say the Georgians, and Russians have been hinting darkly that a land attack may follow. The Georgians stand accused of posing a threat to Russian security because they cannot or will not take effective action against the Chechen fighters, possibly allied with Islamist extremists from elsewhere, who have set up camp in the remote Pankisi gorge. If you cannot solve the problem—and guarantee that no attacks on Russian territory will be launched from Georgian territory—then we will, is the Kremlin's message. The Russian

media, meanwhile, have mounted an escalating series of personal attacks on Georgia's president, Edward Shevardnadze. The clear implication is that nobody in Moscow would shed a tear if, in the turmoil caused by a Russian attack, the leadership of Georgia were to change hands.

If there is one grain of truth in Russia's arguments, it lies in the fact that Georgia, while not a failed state, is one that has had difficulty asserting its authority in its border areas. Indeed in two of its regions—Abkhazia and South Ossetia—the writ of the Tbilisi government does not run at all. Even in other places, it struggles to collect taxes and enforce the law. This is a dangerous state of affairs; where the rule of law is absent, smugglers in drugs, guns and even deadlier things fill the void.

The mote in Russia's eye

But there is also a huge flaw in Russia's argument. If the Georgian state functions less than perfectly—in Pankisi and elsewhere—that is in large part because Russia itself has consistently undermined it. The restive mini-states within Georgia's legal boundaries (Abkhazia, South Ossetia and, to some extent, Ajaria in the south-west) defy the government with the help of powerful friends in Moscow.

By sending 150 or so military advisers to Georgia, America is attempting to bolster the country's security forces. But even that programme has been undermined by Georgian officers with connections in Russia. If Russians are concerned about the security of their southern frontier, they would do better to reinforce Georgia's statehood rather than chip away at it. Georgia is neither a rogue state, nor (as yet) a failed one. Nor do Georgians need outsiders to orchestrate regime change for them. Imitation is a form of flattery, but others should not be duped into seeing parallels where none exist. ■

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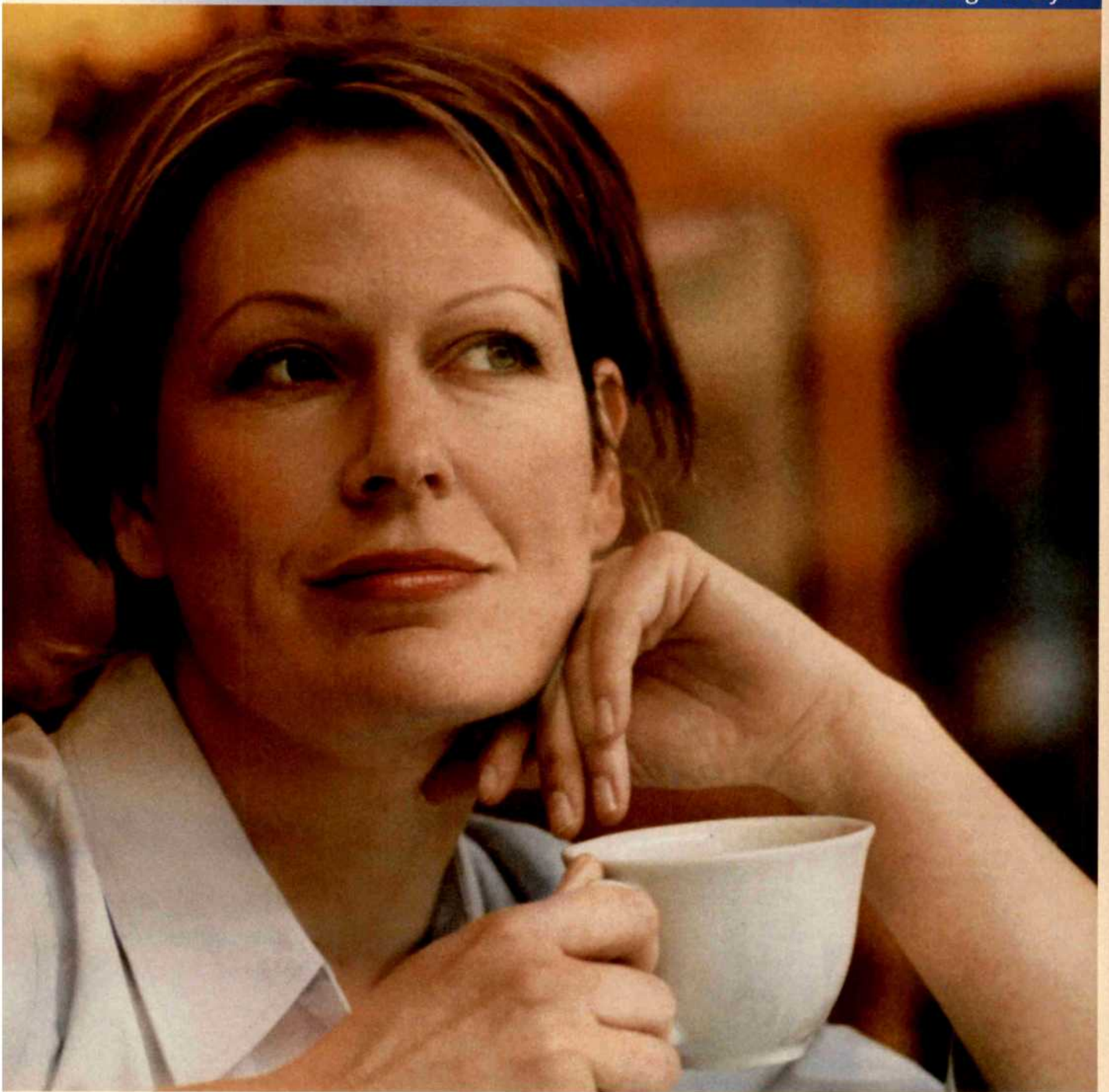
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Who blew the bubble?

SIR – It is hard to agree with your attack on Alan Greenspan and the Federal Reserve (“Greenspan’s bubble bath”, September 7th). If, as you say, America’s liquidity was as generous and unrestrained in the late 1990s, why did the dollar rise? The reasons for the bubble lie elsewhere. Europe is the real culprit. Euro-area central-bank liquidity shot ahead in 1998 and 1999. The new single currency proved a more efficient means of transaction than a dozen national units; consequently, demand fell leading to an excess supply of liquidity in European banks. This launched a tidal wave of European money at popular investments, such as American private equity and tech shares, and significantly weakened the euro.

Big errors in monetary policy come in pairs: for example, in America in 1926-29 (expansion) and 1931-33 (contraction), and Japan 1986-89 (expansion) and 1990-99 (contraction). Worryingly, the European Central Bank has been draining cash from euro-area markets. As expected, domestic economies are slowing and the euro is firming. Yet the ECB, and many pundits, believe that monetary policy is still too loose as nominal interest rates are low and broad-money growth remains high.

Has nothing been learned from Japan in the 1990s? Interest rates measure the cost of credit not the price of money. Sensible people do not want to borrow in a deflation so credit demand and, hence, interest rates are low. Moreover, fast broad-money growth may only tell us that precautionary savings are rising, as shares collapse and economies weaken. In short, the ECB is watching the wrong gauges. It risks steering the economy on to the rocks.

MICHAEL HOWELL
London

SIR – Mr Greenspan’s neglect of duty during the recent stockmarket bubble included ignoring a perfectly effective tool. The Fed has a legal right

to raise and lower margin-account requirements. Margin borrowing is not that substantial but a rise in margin requirements during the day-trading frenzy would have had the same effect as a report of bad earnings or adverse economic data, with the added benefit of issuing a warning signal without restricting credit for legitimate business needs.

L. PAUL NEWBURGH
Los Angeles

Fat of the land

SIR – Americans have a bad diet not because they eat too much fast food, or too much fat and sugar, but because they eat all the time and they eat too much (“Come on in”, August 31st). Calorie intake controls body weight far more than nutrient balance. There is no magic proportion of fat, vitamins, minerals, fibres and sugar in the diet. If you eat too much, do not complain about your waistline.

PIERO DOLARA
Florence

Scotch mist

SIR – Scotland’s “victimhood...an invention” (“Chips with everything”, September 7th)? Do you suppose that Edward Plantagenet took the title “Hammer of the Scots” because he was a handy carpenter? More recent were the highland clearances, but were they not a case of Scottish clan chiefs selling out their own people? No doubt poor journalism has convinced my ruder compatriots that the English were behind this. The third verse of “Flower o’ Scotland”, the country’s unofficial anthem, behoves us to leave history in the past, and to stand up and face the future. Nationalists should remember that.

JOHN SHAW
Paris

SIR – Any belated realisation of inequitable treatment of Scots may be the unmasking of disinformation masquerad-

ing as history. Romanticism, tartans and kilts were not an invention of the Scots who fought for Scotland but largely the result of a 100-year campaign by the establishment, though it failed to hide its direct encouragement of and connection with past horrors and socially destructive commercial investments. The associated campaigns of genocide, levelled largely against the Highlanders and Islanders, caused many to leave Scotland. There is no reason why spelling out the historic facts should create any anti-English sentiment but, rather, will simply set the record straight.

HECTOR MCNEILL
Portsmouth

Kicking Italian football

SIR – Italian football is plagued by long-term problems that you do not mention (“A long dry season”, September 7th). These have been evident for almost a decade but were glossed over by large inflows of television money. The game in Italy is over-dependent on TV revenues. Italian clubs lag far behind those in England and Spain in expanding alternative sources of income, most notably merchandising. While we non-fans decry their number, Manchester United has superstores the world over. English clubs have made massive inroads into Asia in terms of both TV audience and merchandising. Similarly, Spanish clubs have begun to tap vast markets in Latin America, and lately North Africa. Bigger Italian clubs like Milan, Inter and Juventus are trying to redress the balance though, without European success, it may prove difficult.

Italy’s problem in Europe is one of tactical inflexibility. This is a harder nut to crack. In the past two years, no Italian club made the quarter-finals of Europe’s leading competition, the Champions League, simply because they lack the tactical nous to deal with the faster tempo of the Spanish or English game. The excuse? Dark mutterings of conspir-

acy, something shamefully brought to a fever pitch at this summer’s World Cup. I, like most other discerning fans, shall continue to enjoy Spanish and English football.

NARAYANAN RAMAN
Kuala Lumpur

Taxing problem

SIR – Your story on who pays and profits from transportation offers tax-increment financing (TIF) as a glimmer of hope from America (“Getting there faster”, August 31st). In fact, TIF is just another way to privatise profits and socialise losses. In America it is used for such things as building hotel garages that hotels are apparently unwilling to build themselves. Instead, they are allowed to capture the increased property taxes their own property development generates and privatise it at the public’s expense.

Even better, cities with multiple-taxing entities allow some to beggar others. City governments grant TIFs allowing their friends to benefit while school districts, mosquito-abatement districts and other government entities are starved of naturally occurring revenue growth.

TOM YOUNG
Washington, DC

SIR – If governments are to claim tax on increased land values from public investment in transport infrastructure, surely they should also compensate those whose property values fall as a result of pollution caused by increased congestion and emissions, or make up for relative declines in value because of investment elsewhere. Perhaps inhabitants of the north of England should be compensated for policies favouring London and the south-east?

MATTHEW RHODES
Leamington Spa, Warwickshire ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James’s Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com

Executive Focus



New Jersey Institute of Technology

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Executive Focus



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- Strengthen the capacity of the Country Office by adopting, refining and ensuring complementary/integration of existing UNDP initiatives and the identification of new entry points for UNDP/RBA support.

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- Post-graduate degree in Economics. Ph.D. desirable. Excellent oral and writing skills in French and/or English.
- Demonstrated mastery of macroeconomic aspects in the African region and at least ten years of increasingly responsible professional experience in the field of economic development.
- Strong managerial and communication skills. Experience in the development of strategic partnerships.

For further requirements and full job descriptions, qualified candidates are invited to visit UNDP's Website at www.undp.org/jobs (other current jobs) and submit applications by 7 October 2002 at the latest.

CV could also be submitted electronically to leena.dsouza@undp.org or by fax to UNDP Hqts. in New York: (212) 906-6478



**EuroArab
Management School**

EAMS (EuroArab Management School) was established in 1995 in Granada (Spain) by the European Commission and the League of Arab States, with the support of the Spanish Government, to provide education, research and other services for the development of business between Arab and European companies.

The School is looking to recruit suitable persons to fill the following vacancies, all of them starting in January 2003, based in Granada, with occasional travelling assignments:

Director of Research and Academic Affairs

His/Her core responsibility is to oversee, manage and co-ordinate the research activities of the School, as well as the academic components of its various degree programmes.

Research and Teaching Fellowship Programme

Eight fellowships for the duration of twelve months, to carry out research in management, develop pedagogical material and conduct short courses:

The main areas for this programme are:

- SME, Entrepreneurship
- Healthcare Management
- Euro-Arab Political Economy
- Public Administration and Development
- Tourism
- Banking and Finance
- Agribusiness
- Human Resources and Cross-Cultural Management

Interested candidates should submit, before 30 October, a letter of application, updated curriculum vitae, brief description of research and teaching plans (max 2 pages) and two references to EAMS Director General (e-mail: director@eams.fundea.es)

Further information about the vacancies and about EAMS can be found at www.eams.fundea.es or by letter at EAMS, Cárce! Baja 3, 18001 Granada, Spain; phone +34 958 805050; fax +34 958 800152



The Inter-American Development Bank,
the largest regional multilateral development institution, based in Washington, DC, is now reviewing candidates for the positions of:

**SPANISH TRANSLATOR/REVISER
ENGLISH TRANSLATOR/REVISER**

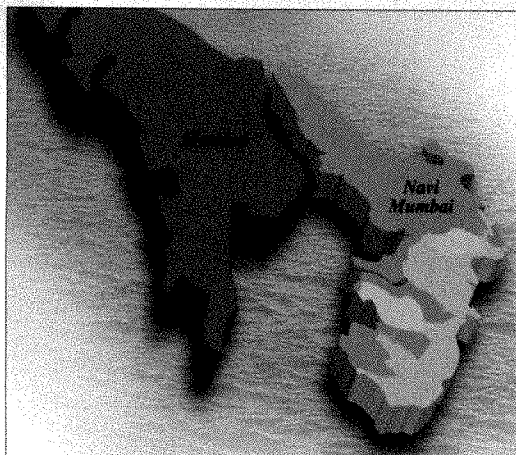
**SECRETARIAT OFFICER
SR. SECRETARIAT OFFICER**

Interested individuals might obtain information regarding the positions' requirements, functions, as well as instructions on how to apply by accessing our Web Site at:

<http://www.iadb.org/hrd/vacancies.htm>

As a reflection of its commitment to its borrowing member countries, the Bank may require staff to accept assignments in both country offices and headquarters. Only candidates selected for interviews will be contacted. The IDB encourages gender equality in its hiring practices.

The Bank offers a competitive compensation package.



Even at a time of unusual products, the offer of a city is admittedly rather out of the ordinary. However, it isn't the nature of its product but rather the nature of the project that asks for your interest.

The City and Industrial Development Corporation of Maharashtra Ltd (CIDCO) is looking for a partner for its latest joint venture. The objective of the new city is to promote exports and attract foreign direct investment. The joint venture will finance,

The new city will benefit from the old.

Geographically, the SEZ-Navi Mumbai enjoys some very special benefits too. It is close to Mumbai and the vast consumer and industrial market that this buzzing commercial metropolis commands. It is barely 25 kms away from Mumbai's domestic and international airports that link it speedily to the world beyond. It is also well connected via a network of highways, expressways and rail corridors, and has one of the most modern mechanized seaports in India.

Close to Mumbai (Bombay), India's vibrant commercial capital, a new city will emerge. The Special Economic Zone - Navi Mumbai (New Bombay) will be a city with just commerce on its mind. It's a city that can be yours - to build, to plan, to market, to own.

plan the infrastructure, market and manage a city that will span 4,377 Ha. CIDCO will take a 26-49% stake in the new company.

The SEZ-Navi Mumbai. A city with the advantages Mumbai never had.

SEZ-Navi Mumbai will occupy a distinctly favoured position. It will function as a duty-free enclave, 'a delineated territory' with hassle-free administration, enjoying a host of special concessions from the Government of India. Full autonomy will be granted for development. The allocation and pricing of land, facilities and services will be left to the JV. It's your city, it's your decision!

The SEZ-Navi Mumbai will be a city inspired by Shenzhen and Jebel Ali. It will be exempt from all taxes, levies, charges and customs and excise duties on the import of capital goods, raw materials and spares. It will enjoy a corporate tax holiday till 2010. Accorded infrastructure status, it will be entitled to all concessions and incentives.

The special privileges abound. Offshore banking units operate freely here. Units will have no minimum export performance, there is only a positive net foreign exchange earning requirement. One step clearances will make operation quick and easy. Supplies from the domestic tariff area will be treated as exports and will thus enjoy important export incentives. So, while the SEZ will be insulated from the domestic tariff area, it will have unrestricted access to it, with sales to the area being permissible with the payment of relevant duties.

Inviting an Expression of Interest

A Tale of Two Cities

All these combined advantages will prove an irresistible lure to units engaged in manufacturing, trading and service activities. Perhaps it is only appropriate that a tale of two cities should be accompanied by great expectations.

International Bidding Process

Prerequisites : The bidders or their promoters, subsidiaries or affiliates should have a Tangible Net Worth of not less than Rs. 250 crores (US\$ 50 million) as per the audited financial results of the preceding financial year. They should have taken part in the construction of or invested in at least one infrastructure project with a total cost of Rs 100 crores (US\$ 20 million) in the last 5 years.

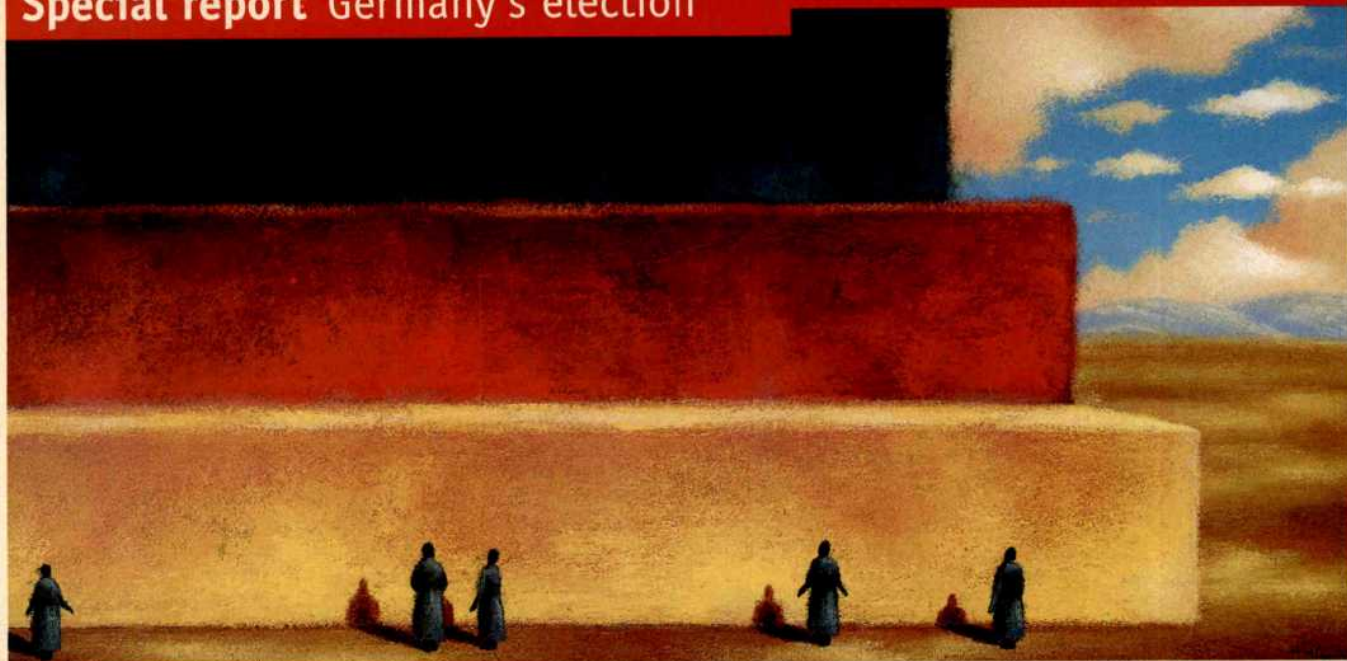
The Process : CIDCO'S JV partner will be selected through an international competitive bidding process. Bidders are invited to provide Expressions of Interest (EOIs) for the project. Short-listed bidders will participate in the second stage of the selection process, either individually or by including new entities and constituting consortia.

The EOI document detailing the selection process and project information may be obtained from CIDCO at the address given below, from 18th September 2002 to 21st October 2002, on any working day, between 10.00 am and 5.00 pm. It can also be downloaded from our website: www.navimumbaizez.com

EOIs must reach CIDCO, at the address given below, by 5.00 pm on 22nd October 2002.

For details, contact:

Anil Kumar Lakhina
Vice Chairman & Managing Director
City and Industrial Development Corporation
of Maharashtra Ltd. (CIDCO)
Nirmal, Nariman Point, Mumbai 400 021,
Maharashtra, India.
Tel: 91-22-2026665 / 2022481 / 2022579
Fax: 91-22-2022509
E-mail: md@cidcoindia.com or cidco@vsnl.com



Giant steps

BERLIN

The parties are neck-and-neck, but neither leader looks up to the challenge of putting Germany right

IT WAS Friday September 13th, the day of the budget debate in the Bundestag, the German parliament. Edmund Stoiber, the conservative candidate for the chancellorship, confidently grasped the lectern. This was his big chance before the election, on September 22nd, to bring the campaign back to the central issue: the dire state of Germany's economy. For nigh on 40 minutes, he harangued the government in an excellent speech full of the most damning facts and figures. Was the country now to go "upwards with the conservatives, or downwards with the Social Democrats?", he thundered in conclusion. Chancellor Gerhard Schröder, his Social Democratic rival, merely laughed. "Mr Stoiber," he sneered, "you may want to become chancellor, but you simply don't have what it takes." The Bavarian prime minister seemed visibly to deflate.

A few hours later it was reported that, for the first time since the beginning of the year, the Social Democrats and their Green coalition partners had overtaken the Christian Democrats and their likely liberal allies in the polls. Only a few weeks ago, most thought they were heading for defeat. Now Mr Schröder's competent handling of last month's floods in the east, and his intransigence over attacking Iraq, appear to have made the difference. The state of the economy, it seems, has been pushed from voters' minds.

Yet not for long. At stake in this election, in Mr Schröder's words, is the fate of "the biggest, most important and economically most powerful country in Europe." Biggest? Yes, in terms of population, which, at 82m, is a third bigger than that of any other EU member. Most important? Possibly, for its geographical position and the size of its GDP, which accounts for a third of the economy of the 12-member euro-zone. Economically most powerful? Hardly.

In fact, Germany has become Europe's sick man. Last year, it managed no more than 0.6% growth, the worst in the EU, after its economy moved into recession (by the standard measure) in the final two quarters. It will probably do no better this year; some growth forecasts are as low as 0.25%. Unemployment has topped 4m and is still rising. Business investment has been falling for seven quarters. Consumer spending remains depressingly flat. The retail trade is in crisis, as is the construction industry. Bankruptcies, 25% higher than last year, are heading for a record 40,000 with the loss of 600,000 jobs.

In the 2002 world competitiveness ratings, compiled by the International Institute for Management Development, Germany slipped to 15th out of 49 countries. For its notoriously inflexible labour-market policies, it ranked among the lowest. Industrial labour costs in western Germany are higher than in any other coun-

try. Germany's tax and social-welfare burden is one of the heaviest in the world. Its share of world trade is falling. Demographic decline is threatening to explode its social-welfare structure. Its health system, the second-most-costly in the world, is under stress. Its schools, once its pride, are failing: Germany came a humiliating 21st in last year's OECD study of the educational performance of 15-year-olds. The country is staggering under a massive public debt. And, despite government denials, it may well breach the EU's 3% budget-deficit limit for euro-zone members this year.

The Schröder score-sheet

Some of Germany's recent economic weakness can be blamed on factors outside the government's control. Not only did Germany lock its economy into the European Monetary Union at what now looks like an overvalued exchange rate, but the European Central Bank's monetary policy is too tight for Germany. Nevertheless, politicians from both parties have done their share of damage.

Mr Stoiber naturally blames his rival for turning Germany into a "basket case". But when Mr Schröder took over from Chancellor Helmut Kohl in October 1998, after 16 years of conservative rule, the country was in some ways in an even worse state. Unemployment was a shade higher than it is now. Germany's debt, taxes and welfare contributions were all at record levels. The labour market, health, pensions and school systems, left virtually untouched throughout Mr Kohl's long reign, were crying out for reform. And the economy, which had been tottering along with average GDP growth of 1.3% a year since unification in 1990, was being slowly suffocated under the same red tape about which Mr Stoiber so loudly complains. ►►

Mr Schröder can be, and has been, sharply criticised for failing to do more. During his term, average GDP growth, at 1.8% a year, has been little better than under Mr Kohl. But he has at least made a start on reform, and it is not inconsiderable. Under his tax reforms, the boldest since the 1950s, corporate taxes have been chopped from 52% to 39%, and the top income-tax rate is being progressively brought down, from a peak under Mr Kohl of 53%, to 42% by 2005. Under the government's less spectacular pension reform, state-subsidised privately-funded pensions have been set up, for the first time, to supplement dwindling state pensions. This new scheme, though inadequate, is at least a basis to build on.

With his five-year *Sparpaket*, or austerity programme, launched in 1999, Mr Schröder has tried to consolidate the country's runaway finances. Under Mr Kohl, public spending had soared to over 50% of GDP. Mr Schröder wants to cut that figure to 42%; so far, he has managed only to lop off a couple of percentage points. But this, too, is a start. He has also halted the steep rise in the public debt, trimming it from a record 61% of GDP, where Mr Kohl left it, to just under 60%. Social-welfare contributions, though still far too high, have likewise been pruned, falling from a peak of 42.3% in 1998 to 40.8% last year—though, squeezed by the economic downturn, they have edged back up since. And although the government appears to have failed to bring the public deficit under control, its long-term aim is still to balance the books, for the first time in 30 years, by 2006.

In other areas, his record is more impressive. Defying strong conservative opposition, Mr Schröder has dared to touch immigration—the first chancellor to do so since the Third Reich. His new law allows urgently-needed foreign specialist workers into the country, while tightening restrictions on others. To help integrate the 7.3m foreigners (including many of the second generation) already living in Germany, the chancellor has also changed Germany's age-old blood-based nationality laws, giving an automatic right to citizenship to anyone born on German soil.



Some lesser reforms are also noteworthy. Mr Schröder has browbeaten Germany's richer states, like Bavaria, into accepting a new €157 billion (\$152 billion) "solidarity pact" to help rebuild the struggling former communist states in the east up to 2020. He has given gay couples the same pension, welfare and inheritance rights as married heterosexuals. He has made a first stab at agricultural reform, trying to wean Germany's 430,000 heavily subsidised farmers away from ever-greater production and into more environmentally-friendly farming practices. He has even taken tentative steps towards labour-market reform by endorsing the proposals of a commission under Peter Hartz, a Volkswagen man, to stimulate jobs and make labour exchanges more efficient.

In foreign affairs, he has presided over democratic Germany's coming of age, leading the country into its first foreign armed conflict since the last world war (in Kosovo) and its first foreign war outside Europe (against al-Qaeda in Afghanistan). On both occasions, he risked the collapse of his government. Germany now has 9,500 troops deployed in international peacekeeping missions, and its forces, though still woefully cumbersome, have begun to be modernised. Mr Schröder's present refusal to offer German support for an American-led attack on Iraq, even if mandated by the United Nations, is a further sign of his country's growing assertiveness and independence, though it also smacks of populist electioneering.

Conservative promises

Mr Stoiber says, of course, that he would do more and better. His key pledge, summed up in the slogan "3 x 40", is to cut public spending, the top income-tax rate, and social-welfare contributions all to un-

der 40%, though he does not say by when. These are not so different from Mr Schröder's own goals (42%, 42% and 40%). At the same time, Mr Stoiber promises to quadruple child benefit to €600 a month for every child under three; abolish social-welfare contributions on jobs earning less than €400 a month; scrap the "green" tax on energy; pump even more cash into eastern Germany; provide more help for small businesses and increase spending on defence, hospitals and schools.

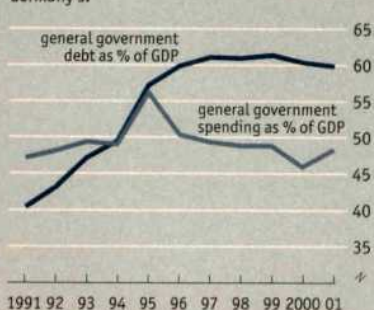
Most Germans doubt whether all this adds up. An economist at the Société Générale bank estimates that Mr Stoiber's programme would cost at least 5.5% of GDP, pushing the public deficit way over the 3% Maastricht limit. Yet Mr Stoiber insists that he would stay within it. "A higher growth rate," he says blithely, "is the solution for all problems." And cutting taxes and loosening the labour market is the way to achieve it, says Lothar Späth, the man designated by Mr Stoiber to head a new super-ministry for economics, employment and eastern reconstruction if the conservatives win on Sunday.

As prime minister of Bavaria, one of Germany's richest and most successful states, for the past nine years, Mr Stoiber has acquired something of a reputation as an economic miracle-maker. Bavaria, once a poor agricultural state, is now one of the most prosperous and advanced high-tech regions in the world, with the highest growth (over the past decade), smallest debt per head, and second-lowest unemployment in Germany. But the state was already flourishing when Mr Stoiber took over in 1993, and he has merely continued the policies of his powerful predecessor and mentor, Franz-Josef Strauss. Mr Stoiber has proved an energetic and efficient administrator, but no great innovator. Transferring his Bavarian policies to the national stage would be harder.

Mr Stoiber maintains that Germany's present economic woes are essentially *hausgemacht* (home-made), and not the results of the world economic downturn, as Mr Schröder claims. But Mr Stoiber may

Hard to cut

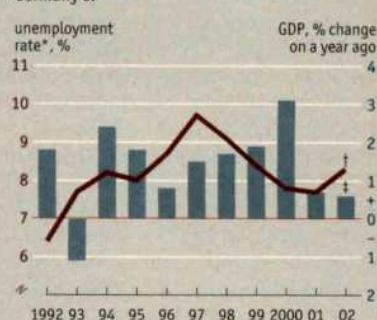
Germany's:



Source: Federal Statistics Office

The sick man of Europe

Germany's:



Sources: Federal Statistics Office; Eurostat; The Economist Poll of Forecasters
* EU harmonised rate † August ‡ Forecast

► have to change his tune now that Bavaria, too, is beginning to feel the pinch of the slowdown. Last year, its economy grew by only 0.9%, making it fifth among Germany's 16 *Länder*, and company bankruptcies soared by 28%.

On paper, Mr Stoiber's proposals look more likely to boost the economy than Mr Schröder's. But he would still find it tough to push through long-term free-market reform, for he is no economic liberal. Like the chancellor (the son of a war-widowed charwoman), he has humble origins: his father started out as a clerk in a building firm, and he sets great store by the "social" element in the name of his party, the Christian Social Union. As the self-styled champion of the "little guy", he speaks up for the *Mittelstand*, Germany's small- and medium-sized businesses; he accuses Mr Schröder, by contrast, of pandering to big business. Mr Stoiber says he wants "productivity and solidarity, individual freedom and social security, self reliance and help for the needy."

A practising Catholic, who proudly proclaims that he has been married to the same wife for 34 years—unlike the four-times-married Mr Schröder—Mr Stoiber promotes old-fashioned family values. He seems to prefer women to stay in the kitchen, despite two lawyer daughters, and opposed the new law on gay rights. He advocates "zero tolerance" on crime and would clamp down on immigration. In the foreign arena, Mr Stoiber is likely to be more pro-American than Mr Schröder. Unlike the chancellor, he has refused to rule out German help for a strike on Iraq.

Eastern drag

Not since 1945 has an election been so hard to predict. Most Germans may not think much of the present government, but nor are they convinced that a conservative one would do much better, especially on the economy. Voters, particularly women and easterners, tend to find the relaxed, punchy Mr Schröder more likeable than his earnest rival, but Mr Stoiber is considered more competent on jobs and the economy. Both get roughly equal scores for intelligence, trustworthiness and credibility. Neither is thought likely to push for radical reform. Mr Schröder is deemed too beholden to the unions, while Mr Stoiber is judged too hand-in-glove with churches, farmers and small shopkeepers. Both are staunch supporters of Germany's "social market economy".

The only proposers of really radical reform are the liberal Free Democrats, who are currently expected to win around 8% of the vote. Some argue, therefore, that any party that is serious about reform would have to include them in a governing coalition. The liberals have not yet said which side they would live with after the election. But after 16 years in coalition with

the Christian Democrats under Mr Kohl, they had little to show for their reforming zeal, and their policies would attract fierce resistance from the unions.

Something bold is needed, however, for Germany's problems go very deep. In a paper entitled "Germany over the next 30 years", the Management Circle, a group of some 1,100 senior and middle-managers linked to the Friedrich-Ebert Foundation, a Social Democratic think-tank, examines where the country has gone astray and sets out the most urgent tasks for the future. After three decades of extraordinary economic success after the war, says Ulrich Pfeiffer, the group's spokesman, Germany began to lose its way in the 1980s. The danger signals were obvious: slowing birth rate, diminishing productivity, spiralling welfare costs, uncontrolled immigration. But Germany, well-off, contented and hard-working, did not think to do anything.

Then came German unification. A region of 16m people, with a clapped-out economy and no modern infrastructure, expected to be raised almost overnight to the level of one of the richest and most advanced nations in the world. The biggest economic mistake, though understandable in political terms, was the setting of an exchange rate of 1:1 for the east German currency against the mighty Deutsche mark. Wages and prices soared, making east German products even less competitive and lengthening the dole queues.

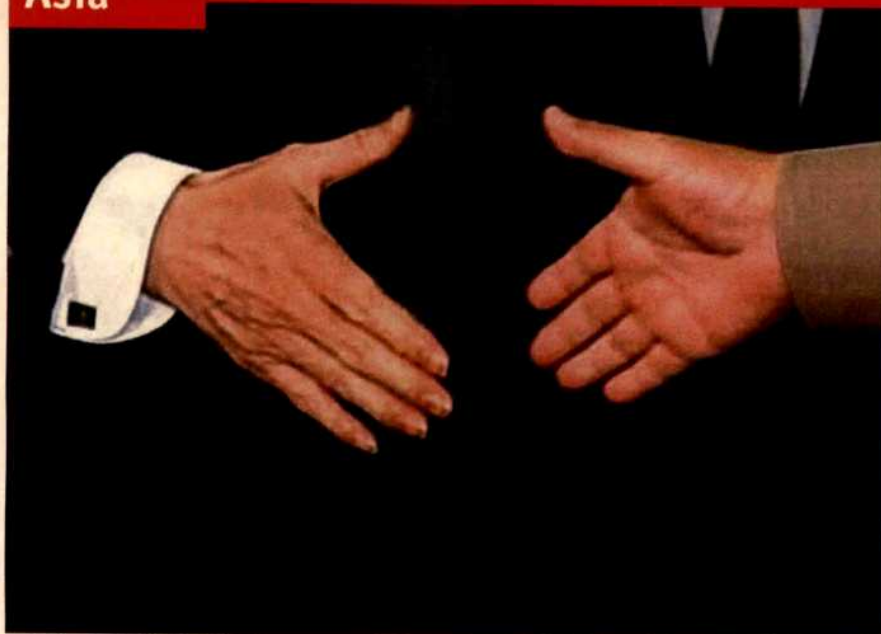
Over the past decade, the region has made huge strides thanks to a massive net public transfer of around €75 billion a year—equal to 4% of German GDP. But productivity and wages still lag some 30% below the west's. Unemployment, currently at 18%, remains more than twice as high. After a post-unification spurt, the region's economy has slowed over the past five years to an annual average of just 1.0%—

half the western rate. Last year, it actually went into recession, shrinking by 0.1%, and is expected to register, at best, no growth this year. An exodus of many of the east's brightest has not helped. Nearly 2m have left for the west since the Berlin wall came down. All this is a burden for Germany which no other industrialised country has had to bear.

Germany as a whole has certainly not been doing well over the past decade. But if western Germany is taken on its own—and it is only this part, after all, that used to be known as Europe's power-house—the recent picture has looked a little less gloomy. In 2000, western German growth—having averaged only 1.2% a year over the past decade—was the same as the EU average of 3.4%. Last year, the world's second-biggest exporter was hit earlier and harder than most by the world economic slump, and western Germany's economy slowed to 0.7%, less than half the EU average. But the downturn is now affecting the rest of Europe. In the first two quarters of this year, western Germany's growth, though still sluggish, was again around the EU average. As for German unemployment, it stands exactly at the EU average of 8.3%, if the harmonised European figures are used and not the much higher German figures. In western Germany the rate is much better, only just above 6%.

Germany is still the world's third-biggest economy, with plenty of world-class companies, a huge trade surplus and a well-trained and determined labour force. But it is no longer fulfilling its potential. Over the past three decades, the problems have been piling up. Germany has already begun to slip behind. What is now needed is a strong, courageous leader who is ready to push through bold, inevitably painful, structural reform. If neither Mr Schröder nor Mr Stoiber appears to fit the bill, this is not just Germany's loss. ■





Japan and North Korea

Not yet friends

TOKYO

Junichiro Koizumi may yet pay a price at home for his trip to North Korea

WHEN its prime minister announced last month that he would make a historic trip to North Korea, Japan was abuzz with talk of a breakthrough on the sorest sticking point between the two countries: the dozen or so Japanese nationals whom North Korea stood accused of abducting in the 1970s and 1980s.

In the event, the revelations emerging from the hermit kingdom on September 17th were more stunning—and more disturbing—than had been imagined. Though there was plenty for the diplomats to get their teeth into, in the shape of a promised extension to North Korea's missile-testing moratorium, and reports of (yet another) promise to re-connect the Koreas by road and rail, it was news of the disappeared that grabbed popular attention in Japan. Junichiro Koizumi's day in Pyongyang—the first visit there by a Japanese prime minister—yielded good tidings for four lucky Japanese families, but relatives of eight other abductees were told, along with a horrified nation, that their loved ones are dead.

One poll showed Mr Koizumi's ratings had surged 10% overnight, but as the news sinks in, some observers fear a backlash that will complicate efforts to reach out to Kim Jong Il's regime. Something similar happened to South Korea's president, Kim Dae-jung, in his dealings with the North. Though North Korea has always denied it, Mr Kim now admits that elements of his

regime did indeed kidnap a number of Japanese nationals, some of them straight from Japan's beaches, and smuggled them back to North Korea. The youngest, Megumi Yokota, who is among the dead but is said to have a surviving daughter born in North Korea, disappeared after badminton practice in 1977, at the age of 13. Mr Kim claims that uncontrollable bits of his regime did this without his knowledge, and used the abductees to teach Japanese language and customs to North Korean spies.

For all the security risks that North Korea poses to its neighbour, the abductions have long been the most emotional and contentious issue in the eyes of most Japanese. Indeed, before this week's visit the worry of many Asian security experts, and especially of Japan's American allies, was that Mr Koizumi might be willing to go soft on Mr Kim in exchange for the public relations coup of bringing a few of the abductees home. Yet even though the four survivors remain in North Korea, and though Mr Kim provided no details about the eight who have died (all, he says, of natural disasters or natural causes, young though they were), Mr Koizumi carried on with the talks before signing a joint statement with Mr Kim that many Japanese may find hard to fathom.

Though Mr Koizumi did not cave in to longstanding demands for war reparations, the statement declares that Japan "honestly admitted the historical facts that

it had inflicted huge damage and sufferings upon the Korean people during its past colonial rule". It then goes on to mention, "in the spirit of the declaration", that Japan will be bestowing some economic aid on its beleaguered neighbour. The statement also mentions that the two sides will "exert all efforts to establish diplomatic ties at an early date". They are already planning for talks to begin next month. Though Mr Koizumi strongly denounced the deaths of the abductees, his decision to carry on making history, rather than turning round and heading home, blurred his message.

With no joint statements to sign, lawmakers back in Japan had an easier time finding their voice. Members of Mr Koizumi's coalition will no doubt be hounding him to learn more about the eight deaths and demanding some compensation for the families, even as he negotiates with North Korea on other issues of aid and security. All of this will tend to complicate Mr Koizumi's job in two different ways in the coming months.

First, he will find his simple one-day excursion into foreign affairs has become a bigger distraction than he counted on. Until now, Mr Koizumi has hardly been a foreign policy prime minister. He chose his first foreign minister, Makiko Tanaka, because of her popularity and her willingness to talk tough to bureaucrats, even though she showed little patience or talent for statecraft. His trips to neighbouring countries have gone relatively unnoticed, and his handful of meetings with George Bush have been designed to show off their friendship while avoiding important issues. Though he will no doubt leave the details of North Korean talks to others, Mr Koizumi must now pay attention to how the reporting of those details could affect his image at home.

Also in this section

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26 China and Tibet

27 Thailand's economy

30 Agriculture in Afghanistan

30 Sri Lanka's peace talks

▶ Restoring that image may also become more difficult. Before his trip to Pyongyang, the betting had been that Mr Koizumi's looming cabinet shuffle will be a mild one, offering few concessions to rival factions in his coalition and leaving him in reasonable control of his team, at least by the standards of Japanese cabinets. But if he carries through with that approach, it will leave him holding more of the blame if a round of by-elections on October 27th goes badly for the party.

He must now hope, therefore, that he can turn the news from North Korea to his advantage, or at least limit any damage, before voters go to the polls. He may yet find a way. He may, for instance, get a boost if and when the four surviving abductees are reunited with their families, though no dates for a reunion have been set. The irony, however, is that Mr Koizumi has already succeeded where his predecessors failed, by returning with precious information about the fate of those who were taken—and yet the truth may hurt him. ■

China and Tibet

Welcoming lamas

LHASA

What lies behind China's charm offensive over Tibet?

SOME gaps are simply unbridgeable, and there are plenty of these to be found in Tibet. Bridges that have been built seem to wash away or fall down quickly. In these spots, the trucks and buses plying Tibet's battered roads must drive down the banks, bump across the river bed, and struggle up the other side. Meanwhile, many of the region's spectacular mountain ravines are simply too dramatic ever to accommodate a bridge of any sort.

There are similarly unbridgeable gaps between China's official account of its magnanimous and tolerant rule in Tibet, and the wrenching tales of thuggery and

oppression told in whispers by frightened, wary locals. China's top official in Tibet, a Tibetan by the name of Legqok, assures visitors that Tibetans enjoy complete religious freedom. But in Lhasa's monasteries and temples, the police presence is heavy, and the talk among monks is of beatings, arrests, and forced political education. Legqok himself is dismissed by many as Chinese stooge.

Since the 1951 takeover of Tibet by Mao Zedong's Communist forces, Tibetans have bristled under (and occasionally, but unsuccessfully, revolted against) their Chinese masters. Staking what it considers an "indisputable" and "ancient" claim to sovereignty over Tibet, China has sought to modernize the place in the hope that rising prosperity, eventually, will be enough to win grudging acceptance by Tibetans of their fate.

There are some signs that this strategy might be starting to pay off. This month, for the first time in nearly a decade, representatives of the Dalai Lama's Tibetan government-in-exile have been hosted—both in Beijing and in Tibet—by the Chinese government. Little has yet been said about it by either side, but the visit, together with a few other recent signs of Chinese softening, has given rise to new hopes that a genuine rapprochement may be on the cards.

Earlier this year, China released six Tibetan political prisoners, and it allowed the Dalai Lama's brother, Gyalo Thondup, to visit Tibet. After years of sharply restricting access to the region by outside observers, Chinese officials have since the summer invited two large groups of foreign journalists on (admittedly heavily-escorted) reporting trips.

According to Thubten Samphel, spokesman for the Tibetan government-in-exile that is based in Dharamsala, in India, the visit of the Dalai Lama's envoys "shows there is some willingness from the Chinese authorities to take steps in the right direction, so from our side we are hopeful that something positive will turn up soon."

The stakes are undoubtedly much higher for the Tibetans, who have looked on helplessly during the past half century of heavy-handed Chinese rule, and now fear, quite justifiably, that their country and its culture are both being extinguished.

China vigorously denies charges that it seeks to change Tibet by flooding the place ▶▶

China and the Internet

The search goes on

BEIJING

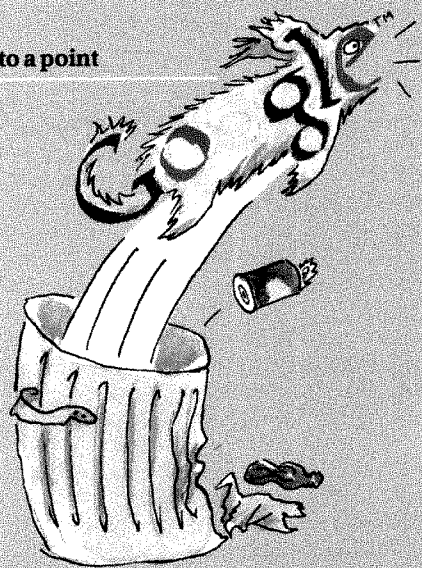
China backtracks on banning Google—up to a point

IN CHINESE, the nickname for Google, is *gougou*, meaning "doggy". For the country's fast-growing population of Internet users (46m, according to an official estimate), it is proving an elusive creature. Earlier this month, the Chinese authorities blocked access to Google from Internet service providers in China—apparently because the search engine helped Chinese users to get access to forbidden sites. Now, after an outcry from those users, access has been restored.

An unusual climbdown by China's zealous Internet censors? Hardly. More sophisticated controls have now been imposed that make it difficult to use Google to search for material deemed offensive to the government. Access is still blocked to the cached versions of web pages taken by Google as it trawls the Internet. These once provided a handy way for Chinese users to see material stored on blocked websites.

After the blocking of Google on August 31st, many Chinese Internet users posted messages on bulletin boards in China protesting against the move. Their anger was again aroused last week when some Chinese Internet providers began rerouting users trying to reach the blocked Google site to far less powerful search engines in China.

Duncan Clark, the head of a Beijing-based technology consultancy firm, BDA



(China) Ltd, says China is trying a new tactic in its efforts to censor the Internet. Until recently, it had focused on blocking individual sites, including all pages stored on them. Now it seems to be filtering data transmitted to or from foreign websites to search for key words that might indicate undesirable content. For example earlier this week when using Eastnet, a Beijing-based Internet provider, a search on Google for Falun Gong—a quasi-Buddhist exercise sect outlawed in China—usually aborted before all the results had time to appear. Such a search also rendered Google impossible to use for several minutes.



Potala imprisoned

with migrants, but it is evident that Chinese migrants are in fact dominating major portions of Tibet's economy; Chinese bureaucrats, as well as soldiers and police, are stifling Tibet's religious and cultural life; and an ambitious Beijing-sponsored development plan, while succeeding in raising the region's standard of living, is at the same time transforming its landscape and browning its unique hues.

The timeless Potala palace survives, but more and more sterile modern architecture is replacing traditional Tibetan buildings, and save for their mountain backdrops, most areas of Tibet's two main cities, Lhasa and Shigatse, are coming to resemble a provincial Chinese town. Despite the sympathy, and cash, that the Dalai Lama attracts to his cause from foreigners, Tibetans, both in Tibet and in exile, know they stand little chance of getting out from under Chinese control. The survival of Tibetan identity may depend on a deal with the government in Beijing.

Though the stakes are far less high for China, a successful Tibet settlement would count as an admirable achievement for any Chinese leader, putting an end to both the internal and international tension that the issue constantly generates.

China's new initiative could simply be an attempt by China's president, Jiang Zemin, to lighten the atmosphere ahead of his scheduled visit next month to President George Bush's Texas ranch. Some experts, however, think there is more to it than that. It may mark Mr Jiang's attempt to secure some sort of political legacy for himself as he prepares to give up at least some of his three official posts in the coming months.

"If this is just a sop to the West, it is going much farther than ever before. All this hints that something much more signifi-

cant is in the works. My hope is that some of the Chinese moderates who have been silenced in recent years are having their voices heard again," says Tom Grunfeld, a Tibet expert, at the State University of New York. Yet, the answer is unlikely to emerge before China's leadership shuffle is complete next year. The likely new president, Hu Jintao, once ran Tibet. Might he be the man to reach a deal with the Tibetans? ■

Thailand's economy

Bubbling along

BANGKOK

The "ifs" that face the prime minister

MANY Thais, stuck in traffic jams on Bangkok's gridlocked streets, console themselves with the thought that the renewed congestion is a sure sign of recovery after five years of economic difficulty and free-flowing traffic. Car sales, at any rate, are zipping along at their fastest pace since the crash of 1997: Thais snapped up 50% more vehicles in August than they did a year earlier. A combination of low interest rates, easy credit and government pump-priming set the economy growing by more than 5% in the second quarter. To fans of Thaksin Shinawatra, Thailand's billionaire prime minister, the figure vindicates the government's controversial policy of "asset reflation". But critics of Thaksinomics argue that the situation is all too reminiscent of the days before the crash: the government is simply nurturing a brand new bubble, they say.

For the past five years, the burden of ex-

cess capacity and bad debts has weighed on Thailand's economy, leaving banks reluctant to lend and firms reluctant to invest. The previous government accepted the conventional economic wisdom that growth would not resume in earnest until the banks and businesses concerned had sold their near-worthless assets, written off their losses and begun to recapitalise. But most businessmen and bankers resisted such steps.

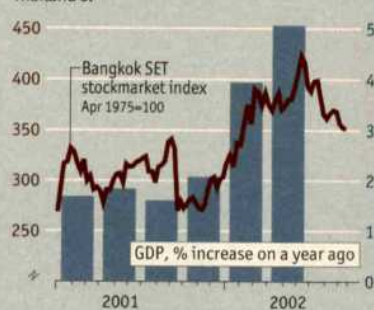
Mr Thaksin took their side, arguing that many investments that looked worthless and loans that looked unserviceable when the economy was stagnant would appear plausible once growth picked up again. Since he took office last year, he has been frantically seeking that growth: providing a soft loan of 1m baht (\$23,000) to every village in the country, subsidising the provision of healthcare, announcing a debt moratorium for farmers, instructing state-owned banks to lend more freely, deferring tax rises, introducing cheap mortgages for civil servants, and so on.

At the very least, this spending was supposed to tide Thailand over until the world economy improved, restoring the depleted demand for exports. At best, it was supposed to alter the country's economy permanently, by strengthening domestic demand as a counterweight to the more unpredictable export cycle. The risk, of course, was that the government would simply rack up big debts, thus pushing interest rates up and the economy down, all for a temporary respite.

So far, however, neither prediction has come true. The reflation has gone just as Mr Thaksin envisaged: property values, the stock market and consumer confidence all shot up in the first half of the year, while private consumption grew robustly. But bad debts remain stubbornly high, and investment sluggish. There is little to suggest that the government's spending spree has launched the economy on a virtuous cycle, according to Ammar Siamwalla, a local economist. Yet fiscal ruin is hardly at hand. This year's deficit is likely to fall short of the budgeted 3.8% of GDP. Next year's auspicious 999.99 billion-baht ▶▶

Bouncing back

Thailand's:



Sources: Bank of Thailand; Thomson Datastream

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THE RELENTLESS PURSUIT OF PERFECTION

budget reins in spending further. Supavud Saicheua, an economist with Merrill Lynch Phatra, an investment bank, argues that public debt will remain manageable as long as the economy grows by 4% or so.

If the economies of the United States and Japan, Thailand's biggest export markets, pick up next year, the government can continue to reduce spending, without bursting its own bubble. But if, as is equally plausible, a war in the Middle East pushes up oil prices dramatically, or exports contract, or healthcare costs run out of control, Mr Thaksin will face the choice of slashing spending or allowing interest rates to rise—and doing so in the run-up to parliamentary elections in 2004. That would really leave the prime minister and his countrymen in a jam. ■

Agriculture in Afghanistan

The gardens of Eden

Fighting the drought, and the looters

FOR Abdul Hakim, gardening is a family tradition. As his father and grandfather did, he works in the gardens of Nimla Bagh, in Nangarhar province in eastern Afghanistan, which are said to have been laid out in the 1630s as a Persian recreation of Eden. Three years of drought, however, have left their mark on Nimla Bagh, as well as on the country's once prolific orchards and fields. Irrigated areas have shrunk by more than half since 1978, turning a country that was approaching self-sufficiency into a big importer of grains, fruit and vegetables. Restoring Afghan agriculture will be a long task.

Afghanistan's terrain, climate and tradition of gardening make it a good place for growing fruit. In the 1970s, export of fruits and nuts provided about 40% of the country's foreign exchange. About 60% of the world's dried fruit came from Afghanistan. In the 1990s the Food and Agriculture Organisation (FAO) helped to create over 300 fruit-tree nurseries throughout the country to replace orchards destroyed during a decade of occupation by the Soviet Union. Further fighting ruined more of Afghan agriculture, including the vineyards of the Shomali plain. But it was the lack of water—and the lack of money—that devastated the country's orchards, most of which are now in a sorry state. Such fruits and vegetables that are produced are difficult to distribute or export because many of the country's roads and bridges have been destroyed.

Food crops that need less water, such as wheat, are doing better, although the FAO

estimates that the revival of poppy growing for opium since the defeat of the Taliban has reduced the area of irrigated wheat by some 10%. The good news is that over the past few months rains have returned to some parts of the country, and food supply should improve. Afghanistan should produce 3.6m tonnes of cereals this year—82% more than last year, but still 4% less than in 1998. Yet about 6m Afghans, (the poor, the displaced, and the masses of refugees who have returned) will still need food aid during the coming months. And it will take a lot more rain to replenish the country's low water table.

It was reported last week that the national seed collection, which reflected the genetic diversity of the country's major crops, had been destroyed by looters who broke into offices in Ghazni and Jalalabad where the seeds were stored. The thieves took the plastic containers and threw the seeds away. However, there is hope for a recovery: since July scientists have been collecting samples of pistachio nuts, almonds and melon seeds. And once the country becomes safer, says Nasrat Wasmisi, who heads an international group working on reviving Afghan agriculture, the seeds collected in the 1960s and 1970s and now kept abroad will be repatriated.

In the meantime, the FAO is helping to repair irrigation systems, distributing seeds and surveying those tree nurseries that are worth reviving. In Nimla Bagh, Abdul Hakim is still counting the useful trees remaining in the vast gardens. "My grandson counts beside me," he says, "and that gives me hope." ■

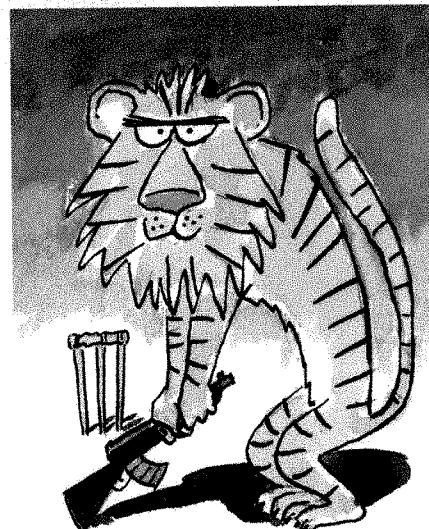
Sri Lanka

Friendly Tigers

Peace talks begin with a purr

SO FAR, so good. Sri Lanka's government, representing the penitent chauvinism of the country's Sinhalese majority, this week met the ex-terrorist, ex-separatist Liberation Tigers of Tamil Eelam for talks in Thailand aimed at ending the country's 19-year civil war and agreed to talk some more. Both sides had modest agendas for their first direct negotiations in seven years: to continue the normalisation of life in the north-east, which the Tigers claim as the homeland of Sri Lanka's Tamil minority, while skirting touchier issues such as just how the region will be re-integrated into Sri Lanka.

With the help of Norwegian facilitators they succeeded. They set dates for three further rounds of talks. The next begins on



October 31st. Meanwhile, the government and the Tigers will set up joint committees to deal with such issues as rebuilding the north-eastern battleground, which the Tigers partly control, starting by removing landmines and resettling hundreds of thousands of displaced people. They also discussed swapping prisoners of war. These agreements will reassure donors that the peace is hardy enough to warrant stepping up aid to the region.

Nonetheless, each side is handling the newborn tenderly. The government, eager to end a war that has killed 65,000 people and stunted economic growth, has tried to steer well clear of issues that might inflame Sinhalese nationalists, still unreconciled to making peace with the Tigers, or that could provoke the Tigers themselves. So there is little discussion yet of just what powers will be granted to a Tiger-dominated provisional administration for the north-east. The Tigers also sound accommodating. Anton Balasingham, their chief negotiator in the Thailand talks, said more plainly than the organisation has previously conceded that it would settle for something short of an independent state.

The Tigers seek regional autonomy, he said. Separation would be a last resort. Since the government has said it will consider any solution short of independence, the negotiations now look safe from collapse at least over this basic principle. If the Tigers are to pull out at any stage they will have to come up with another reason.

Already there is a peace dividend. Both sides are improving their adherence to the terms of a ceasefire that formally began in February. The Norwegian-led Sri Lanka Monitoring Mission reports that violations of the ceasefire fell by 28% between July and August. Shares on the Sri Lankan stock exchange touched a five-year high this week. A dozen foreign cricket teams have come to Colombo, the capital, for a tournament—more evidence, says the government, that peace is paying off. ■



George Bush and Iraq

Your moves

WASHINGTON, DC

The president's speech to the United Nations about Iraq may transform domestic politics as well as international diplomacy

GEORGE BUSH has pursued almost exactly the same gambit to persuade Congress and the Democrats to back his Iraq policy as he has used to twist the arms of European and Arab allies. The move seems to be working slightly better on the foreign board than the domestic one.

In both cases, the president began by staying silent while criticism of American unilateralism began to erupt around him—from “friends” abroad and members of his father's administration at home. This encouraged Democrats at home and sceptical allies abroad to demand a big debate about Iraq before committing themselves.

Next, someone conveniently leaked an opinion from White House lawyers that claimed the president did not need Congress's authorisation to go to war, even while the vice-president, Dick Cheney, was alarming the United Nations by publicly dismissing weapons inspectors as providers of “false comfort”. This naturally provoked Congress and the UN into demanding their say.

Then, with pressure building up on what were really procedural matters (do we consult the UN?) not substantial ones (should we attack Iraq?), Mr Bush calmly pulled the rug from under his critics' feet. By taking his case to the UN and Congress,

he conceded the procedural points without giving an inch on the substance. This put the onus back on his opponents—demanding the UN put inspectors back in, demanding Congress pass a resolution, and forcing Democrats to respond on the merits of his case against Iraq.

That does not mean that Mr Bush has won the game—particularly on the foreign board. His speech to the UN was initially greeted with praise for the case he made and some relief that he had couched it in terms of international law and UN agreements. Saudi Arabia, for instance, offered the use of its Prince Sultan airbase for any UN-backed operations. But there was a catch: what operations?

By offering to accept the current inspections regime before a tougher one could be agreed upon, Saddam Hussein then managed to split the UN Security Council and plunge it into discussion about the devilish details of the inspectors' remit. Russia's foreign minister, Igor Ivanov, said: “We don't need any special resolution for [inspections] to occur. All the necessary decisions about that are to hand.” His French peer, Dominique de Villepin, initially took that view too, though he later backtracked a bit. America, by contrast, is adamant that the current inspections regime is too lax.

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Under the latest UN resolution, number 1284, issued in December 1999, the inspectors would have 60 days to draw up a schedule of the steps towards disarmament that Iraq must take. Four months after fully satisfying the inspectors, and setting up a monitoring system, sanctions could be suspended.

The administration maintains that the inspectors can have no idea what weapons Iraq has, since they were booted out four years ago. It wants Iraq (not the inspectors) to draw up a list of what it has; then the inspectors will check it, with even the smallest unaccounted-for weapon being a breach. And it says that the current regime has too many loopholes—for instance, it puts conditions on the inspection of so-called “presidential” sites.

There is also a timing problem. Some of Mr Bush's people think that, because the inspectors have been out of Iraq so long, it could take a year or more to satisfy the current demands. Though America still needs time to assemble its forces in the Gulf, it does not want to wait a year. For all these reasons, the administration is now trying to get the Security Council to pass a new resolution with tougher conditions for Iraq in the teeth of Russian objections.

America's case may not be deadlocked at the UN. Forced to choose between Iraq and America, Vladimir Putin would surely not back a dictator who owes him billions or risk American condemnation over Chechnya. But for the moment, Mr Hussein's ploy has brought closer an unenviable choice for Mr Bush: if he cannot get the UN to agree to tougher inspections, he may have to disregard the UN after all.

At home, Mr Bush's speech has worked ➤

▶ better. Its first effect was to unite his own party. Immediately after the speech, two leading senators, Trent Lott and John McCain (who rarely see eye to eye on much), issued a ringing endorsement of Mr Bush and called on the Senate to pass the required congressional resolution forthwith. Chuck Hagel, one of the leading Republican critics of unilateral action, backed them.

Less predictably, Mr Bush's speech forced Democratic leaders in Congress into line. After previously saying there was no hurry to get a resolution passed before Congress's session ends in October, Tom

Daschle, the leader of the Senate, finally said yes, Democrats would vote for a resolution supporting possible use of force in Iraq. As *The Economist* went to press, the White House was due to send a draft resolution to Congress.

From an electoral viewpoint, this has forced the Democrats to adjust their position. Their basic Iraq strategy had been to change the subject. Almost no Democrat opposes regime change in Iraq, but few want to talk about it because they think it distracts from their favourite domestic issues—Social Security, prescription drugs and so on. Edward Kennedy was open

about this: "We can't let it [Iraq] replace the domestic agenda."

When they haven't been able to change the subject, the Democrats have tried to obfuscate. Some have accused the White House of "wagging the dog": in the words of the director of the Senate campaign committee, "the administration has timed the Iraq public-relations campaign to influence the mid-term elections". (If polls are any guide, few Americans believe this.) Others, like Dick Gephardt, the party's leader in the House, have argued that Mr Bush must explain how attacking Iraq fits into the war against terrorism and give more details on Iraq's nuclear weapons. Still others say America should not go to war without a new UN resolution.

These are legitimate issues. But as a political strategy they have been destroyed by Mr Bush's dual approach to the UN and the Congress. The Democrats have been left nit-picking about procedures. This may be understandable: without the intelligence reports available to the president, few people are willing to contradict his claim that Mr Hussein is a danger to the world. In this form of asymmetric politics, the president has the advantage. But that does not lighten the Democrats' burden. The congressional resolution will pass, perhaps overwhelmingly.

That leaves the complicated question of the November mid-term elections. The Republicans are clearly seeking to use Mr Bush's popularity (which is now going up again) to turn the elections into a referendum on him, and on Iraq. He seems happy to lend his prestige to stump speeches for Republican candidates. Advertisements on Iraq have started to crop up in local races and Republicans are circulating Democratic votes in the resolution before the 1991 Gulf war (most voted against).

This is a risky ploy because domestic debates about war have not usually been partisan affairs: politics is supposed to stop at the water's edge. Mid-term elections have anyway tended to be referendums on domestic matters. Republicans can thus refer to the war—but not in such a way that it looks as if they are trying to score partisan points (even when they are).

For their part, Democrats, having lost the Iraq debate, must find a new way to emphasise the domestic agenda. The congressional resolution might come early enough for voters to have forgotten about it by November 5th. More likely, though, Democrats will have to hope the mid-terms are not a national election at all, just a series of local races.

It is unclear whether the races will be "nationalised". But on current trends, Republicans do not look likely to lose more than a handful of seats at worst—defying the usual mid-term reaction against the party in power. For that, the Iraq debate must be partly responsible. ■

Al-Qaeda

The fifth column

LACKAWANNA, NEW YORK

A sleeper cell is supposedly discovered in upstate New York

IN THEORY, it was a good week in America's war against al-Qaeda. In Pakistan, the authorities arrested Ramzi bin al-Shibh, the alleged mastermind of the September 11th attacks: he will probably go to join other terrorist suspects in Guantanamo Bay. The FBI also picked up six alleged members of an al-Qaeda cell based in Lackawanna, near Buffalo, on the New York-Canadian border.

Yet, for many Americans, the news from Lackawanna is a grim reminder of al-Qaeda's omnipresence. The steel town, though down on its luck, has an all-American feel, with well-kept clapboard bungalows and plenty of patriotic flags. The suspects—five of whom were picked up in the town, the other one in Bahrain—are of Yemeni descent; but they were all born in the United States and went to the local high school. One was voted the friendliest in his class; another worked as a security guard at a home for troubled children. All were registered to vote—as Democrats.

No weapons or explosives were found when their homes were searched. The main, circumstantial, evidence against them is that in 2001 they travelled to Pakistan for the same extreme form of religious training received by John Walker Lindh, the so-called American Taliban, and Richard Reid, the accused shoe-bomber. According to one suspect, four of them then went on to an al-Qaeda camp for weapons training and a pep talk by Osama bin Laden.

It is not clear why the authorities pounced this week. The FBI had been monitoring the young men even before last September's attacks, and had pulled in at least one of them several times for questioning. In July, the bureau intercepted an e-mail that mentioned possible terrorist activity.



Seems innocent enough

The arrests came a few days after a code-orange warning, indicating a high chance of a terrorist attack. Increasingly, the authorities are under pressure to move pre-emptively. This week, Senate hearings revealed that the intelligence services were warned that al-Qaeda might use aircraft as weapons before last year's attack, but did little about it.

The arrests follow similar round-ups elsewhere. Last month, five men, including three Moroccans and an Algerian, were arrested in Detroit for conspiracy to provide material support to terrorists. Two Lebanese brothers in North Carolina were convicted in June of helping to run a support cell that funnelled cigarette-smuggling profits to Hizbullah.

But the arrests are still a shock for Lackawanna, which has long had a small community of Yemenis (originally, they came to work for Bethlehem Steel). The mayor says that his first reaction was: "Not in my backyard." He may not be the last mayor to be surprised.

Fiscal policy

Deficits, dividends and discretion

WASHINGTON, DC

The present is better than it looks; the future may be worse

HOW well off is the American government? The answer depends on the timeframe. From a long-term perspective, the government's finances have taken a hit. When George Bush entered the White House, the Congressional Budget Office (CBO) expected surpluses of \$5.6 trillion over the next decade. Now the forecast is for a surplus of around \$1 trillion by 2012—and that is only if you assume that Mr Bush's tax cuts will expire in 2010, something they are formally supposed to do, but few politicians believe will happen. In practice, those tax cuts, coupled with a falling stockmarket and Congress's appetite for spending, have eaten up the surplus.

On a short-term view, though, the picture is different. Fiscal loosening has helped prop up the faltering economy. Indeed, with state budgets tightening, interest rates at historic lows and the recovery still looking anaemic, some on Wall Street think that a greater fiscal stimulus may be necessary.

According to the Bush team, the right sort of fiscal policy is to control spending now and cut taxes in the future. Mr Bush has happily signed plenty of expensive laws, including \$86 billion in new farm subsidies over the next ten years, and only this week the White House warned that a war with Iraq might cost \$200 billion. But the president makes much of Congress's profligacy. In August, he pointedly refused to sign a bill that contained \$5.1 billion in "emergency spending", which he deemed unnecessary. Just this week, he berated Senate Democrats for their lack of budget discipline.

Mr Bush believes that the best boost for America's drooping economy is to make last year's tax cut permanent. Others want an immediate round of tax cuts too. Larry

Lindsey, Mr Bush's closest economic adviser, is championing a package of measures designed to help beleaguered stock-market investors. The economic merits of these ideas are mixed. One idea—reducing the double taxation of dividends—would improve the tax code. Another—allowing people to put more money into tax-preferred retirement accounts—might boost saving, but that would mean that consumers spent less in shops now.

The main point of talking about such tax cuts is political. Even Mr Bush's supporters agree that tax cuts for investors would have virtually no chance of congressional passage before November's elections. The idea is to give Republicans something to offer investors, though some congressional Republicans worry that they would be accused of pandering to the rich.

A sinking ship?

That would certainly be the Democrats' position. They have blamed the worsening deficits on Mr Bush's tax cuts, often in dramatic terms. Kent Conrad, the chairman of the Senate Budget Committee, says the president is "punching more holes in the hull as the ship goes down."

Despite their claims to fiscal probity, only a minority of Democrats (including two presidential hopefuls, Joe Lieberman and John Edwards) have argued that the tax cut should be delayed or rolled back. And the Democrats have made no effort to scale back their spending plans, which include expensive prescription-drug benefits for older Americans.

Alan Greenspan has also weighed in. There is plenty of fiscal stimulus already in the pipeline, argues the chairman of the Federal Reserve: the real risk is that Congress may abandon fiscal discipline entirely. Avoiding this fate does not mean rolling back Mr Bush's tax cuts (which Mr Greenspan famously endorsed last year), but depends on controlling spending. Mr Greenspan wants a raft of budget rules that were introduced in 1990 and are due to expire on September 30th to be extended. These rules set explicit caps on discretionary spending (the money that lawmakers appropriate every year) and demand that tax cuts or policy increases in mandatory spending, such as on Medicare, be paid for by cuts elsewhere. In Mr Greenspan's view, these rules helped push down discretionary spending from 10% of GDP in 1990 to 6.5% by 1998.

At least some of these budget rules may eventually be extended. But a return to the discipline of the 1990s looks unlikely. There is no strong consensus for deficit reduction now, as there was a decade ago. Despite some politicians' apocalyptic language, America's fiscal position for the next few years is relatively comfortable; indeed, it is still stronger than in many other industrial economies (see chart). With

global growth weak and deflation a risk, an obsessive focus on deficit reduction in the short term would be misplaced.

The medium term is cloudier, but not disastrous. The official budget forecasts of a return to surpluses by 2006 look too rosy: they make unrealistic spending assumptions and ignore unavoidable tax changes, such as fixing the Alternative Minimum Tax, which will affect a third of all taxpayers by 2010. Yet even with more realistic assumptions about spending and tax policy, a return to the huge deficits of the early 1990s (which peaked at 4.7% of GDP in 1992) seems unlikely.

Yet this relative fiscal health masks a long-term problem that begins to bite at the end of this decade: the ageing of the baby boomers. According to a recent study by the CBO, spending on entitlements—pensions and, particularly, health care—will soar from 7.6% of GDP in 2000 to 11.3% by 2020—and that is without any new expensive prescription-drug benefits. By contrast, discretionary spending is only 7.1% of GDP and is supposed to fall (admittedly according to those optimistic figures) to 5.7% by 2012.

This underlines an important point. America's long-term fiscal health depends less on controlling discretionary spending (the current focus of Mr Bush) than on controlling entitlements. As Bob Reischauer of the Urban Institute puts it, even the strictest controls on discretionary spending will be a "rounding error" in the overall budget problem of the future. ■

The California governor's race

Blues of the Greens

LOS ANGELES

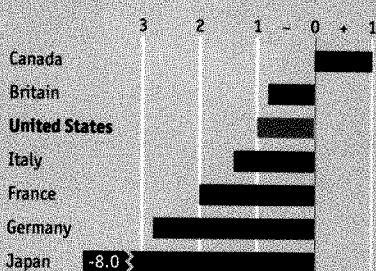
An invigorating candidate is unjustly pushed to the sidelines

PETER CAMEJO hates to be called a spoiler. As the Green Party candidate for governor of California in the election on November 5th, he is often warned that he could end up helping Bill Simon, the Republican candidate, to defeat Gray Davis, the incumbent. That, claim his Democratic detractors, is exactly what Ralph Nader did to Al Gore in Florida.

On the face of it, there is no danger of that happening in California. A Field poll released on September 5th gave Mr Davis a lead of seven percentage points over Mr Simon, considerably larger than the 3% of voters who supported Mr Camejo. But the poll also showed 22% undecided, a share that has risen—at a stage in the campaign when opinions would normally be becoming firmer, not softening—from 16% in July. And both the main candidates have ▶▶

Not so bad

Budget balances as % of GDP*, 2002 projections



Source: OECD

*Includes social-security balances

► higher negative than positive ratings.

That makes Mr Camejo a potentially dangerous man as far as the governor is concerned. It is a familiar position for him; back in the 1960s, when he was a leader of the student radicals at the University of California at Berkeley, the governor of the day, Ronald Reagan, named him one of the ten most dangerous men in California. As a first-generation Venezuelan-American, Mr Camejo could broaden the appeal of the Green Party among Latino and minority voters who, up to now, have disproportionately backed the Democrats. According to Mike Madrid, a Republican consultant, one-third of Latinos say they dislike both candidates from the main parties—the highest share ever to do so.

That threat and potential explain a lot about what happened in Beverly Hills on September 17th, when Mr Camejo and Mr Simon—but not Mr Davis—took part in one of the only debates of the campaign. Showing up to a debate with Mr Camejo would not help the governor (who has agreed to debate Mr Simon only once). Mr Davis would have had to bear the brunt of Mr Camejo's attacks, and his presence would have guaranteed more media attention.

The audience for the debate was small; but it was both larger than Mr Camejo can normally reach and slanted to groups he hopes to impress, ethnic-minority businessmen and media folk. Mr Camejo duly stressed not only environmental issues but education, workers' rights (including a minimum "living wage"), universal health-care and a shift away from "three-strikes" laws towards rehabilitation—all of which may well endear him to poorer Californians. For good measure, he also got in many a dig at corporate crime.

Yet Mr Camejo is no anti-capitalist. He founded Progressive Asset Management, a financial advisory firm that applies stringent environmental, social and ethical criteria to investment. Mr Simon's background is also in investment management (to his delight, a fraud verdict against his family investment firm had been thrown out of court a few days earlier) and the two financiers were positively fulsome in their gratitude to each other for showing up. A common enemy is a wonderful bond.

Mr Camejo knows he has no chance of winning, nor even, probably, of helping Mr Simon to win. At best, his campaign may raise the profile of the Greens a little. California already has 51 Greens in local offices, including four mayors. Michael Feinstein, the Green mayor of Santa Monica, notes that many local elections employ systems such as instant runoff voting, approved this year by San Francisco, that give minor parties a greater say. Mr Camejo wants IRV extended statewide. He still wouldn't win, but at least Mr Davis might deign to debate him. ■

The Massachusetts primary

Waiting for Mitt

BOSTON AND WASHINGTON, DC

The year of the female governor? Or of the Olympic organiser?

SHANNON O'BRIEN had reason to look drained on September 17th, after she finally won Massachusetts' Democratic primary for governor. Throughout most of the long campaign, the state treasurer had been the frontrunner and thus continually battered by three feisty opponents—Robert Reich, who was Bill Clinton's labour secretary, Tom Birmingham, the president of the state Senate, and Warren Tolman, a former state senator. Now she faces an even tougher challenge in Mitt Romney, the Republican candidate.

In the end, nothing that Ms O'Brien's rivals threw at her would stick. When her opponents noted that the value of the state pension fund she oversees had plummeted in recent months, voters looked at their own sagging mutual funds and decided it wasn't her fault. When rivals pointed to her less than swingeing views on gun control, voters decided it didn't trump her liberal stances on other things.

In fact, Ms O'Brien and her opponents shared the same leftish views on most issues. The primary battle seems to have been decided on the basis of personality and the ability to bring out the voters in a year of dismal turnout. Ms O'Brien had the advantage of a strong field operation; she comes from a prominent political family, and she was the only candidate to have won a statewide race. She was also the only woman in the race. Women favoured Ms O'Brien over her male rivals, by a mar-

gin of nearly two-to-one.

If she wins, Ms O'Brien would become Massachusetts' first elected female governor. (The current, somewhat unpopular Republican incumbent, Jane Swift, was elevated to the position from lieutenant governor—and is not running again). Ms O'Brien's success was duly hailed the next day by Emily's List, a women's group that supports abortion rights, which wants this to be "the year of the woman governor". There are only five at the moment, and three are leaving office; but nine are running this year, including Jennifer Granholm in Michigan (see Lexington).

All very inspiring; but first Ms O'Brien must get past Mr Romney. The businessman, who is as handsome and fluent to his supporters as he is artificial and glib to his opponents, has a big lead in the polls and brimming campaign coffers. He has used his successful stewardship of the Winter Olympics to pitch himself as an outsider. As Ms O'Brien celebrated, Mr Romney mocked her years in government and appealed to supporters of Messrs Reich and Tolman, who had dubbed themselves reformers, to join "another team that's willing to go up against the insiders."

With Republicans accounting for only 14% of the Massachusetts electorate, Mr Romney needs crossover votes. His main targets are independent voters who make up nearly half the electorate. To lure them, he will call in help from the Bush family, while Ms O'Brien will bring in Bill Clinton and Senator Ted Kennedy. Mr Kennedy clobbered Mr Romney in 1994, by painting him as an uncaring businessman who didn't understand working-class needs. But Mr Romney is a more polished act nowadays, and Massachusetts is far more annoyed with its political establishment. The rested Olympian outsider should see off the exhausted female insider. ■



One half of the marathon completed

The victims' fund

De factos of the matter

NEW YORK AND CAMBRIDGE, MASSACHUSETTS

New York's first amendment: don't stiff the rich, they tend to sue

IN PRINCIPLE, it was a great idea. Last September, Congress passed a bill creating a federal fund to compensate the families of the victims of the September 11th attacks. They were encouraged to sign up with the promise of quick, guaranteed payments, and the fund was supposedly unlimited in size. In exchange, claimants had to waive their right to sue for damages in civil suits stemming from the attacks.

Things are not working out as planned. Few of the eligible families have filed claims to the fund. Of the 43 awards that have been offered to families, five are being contested. Now Cantor Fitzgerald, a bond-trading firm that lost 658 employees in the World Trade Centre, has filed a brief to the fund's master, Kenneth Feinberg, saying his terms are unjust and illegal.

Like many of the victims, Cantor thinks the fund is paying less than the courts would. Payments from life insurers or pension funds are deducted from the fund's award, though a court awarding damages in a wrongful-death suit would not "offset" payments in this way. The fund also calculates its awards after deducting tax, while New York courts award tax-free amounts. And Cantor in particular claims that, because its business was booming, its employees would have made far more money than the fund thinks.

The angriest families are the richest ones. If a victim was even modestly wealthy, the "offset" rule alone probably wipes out most of the award that the fund might offer. Because of the way the awards are computed, all the families of victims with incomes above the 98th percentile in the national averages may well be offered the same amount, even if the victims' incomes were wildly different. Cantor also claims that, despite Congress's assurance that there would be no cap on the awards, both the rules of the fund and comments made by Mr Feinberg suggest that a de facto cap exists.

By ignoring the financial profile of the victims, Mr Feinberg has created a situation where a tenth of his constituency has nothing to lose by fighting him. Cantor's death toll alone includes more than 250 people whose incomes were above the 98th percentile threshold. Cantor's boss, Howard Lutnick, is a notoriously litigious man. His firm's report lays out a long list of reasons why Cantor families may be able to challenge the fund in court. Another group of victims' families is trying to coax

Barely legal rural pursuits

Cock and bull

HOT SPRINGS, ARKANSAS

An old sport survives

GAME-BREEDERS who raise roosters for cockfighting are secretive and sensitive souls. When they gather for their annual convention (this year, at the Arlington Resort Hotel and Spa in racy Hot Springs, Arkansas), they do not want media intrusions. That is because the sport they supply is not always on the right side of the law.

Cockfighting, better known as the "sport of kings" (at least in these kingless parts), is legal only in Oklahoma, Louisiana and New Mexico. In 27 states, it is a felony. Where cockfighting is illegal, it has naturally gone underground—or rather, on to the back-roads and into dusty fighting pits in corrugated-iron sheds. There, two gamecocks, armed with razor-sharp gaffs and often drugged, are placed in a pit to attack each other, while spectators gamble on the outcome. One bird is usually killed;

**You calling me chicken?**

a bill through Congress that would eliminate the offsets for other income and remove the cap on pain-and-suffering awards made by the fund.

Meanwhile, the civil suits are mushrooming as well. The office of New York city's Corporation Counsel has hired two dozen new lawyers to defend against claims that it fears could reach into the billions. Just before the one-year deadline on filing wrongful-death suits expired, more than 1,000 plaintiffs filed a civil lawsuit against the Port Authority of New York and New Jersey, charging it with negligent construction and maintenance of the twin

sometimes both are. The sport is popular, especially among Latinos, and the police have a hard time stamping it out.

In Arkansas, where cockfighting was banned in 1879, the sport still flourishes. (It is only a misdemeanour under Arkansas law, but a proposal on November's ballot seeks to have it re-classed as a felony.) Two of America's biggest cockfighting magazines—the *Feathered Warrior* and the *Gamecock*—are based there. The barkeepers of Hot Springs are happy to take the dollar of the United Gamefowl Breeders Association (UGBA). And hundreds of Arkansas farmers raise the birds, inbreeding them to make them more aggressive, for sale across the state line.

Earlier this year, Congress passed an act that outlaws interstate shipping of game birds for sports such as cockfighting. It comes into force in May 2003, and already ways are being found round it. Some poultry farmers simply say they will defy the law and go on shipping birds. Several have already started smaller farms in Louisiana where they plan to raise chicks for profit. They also ship birds to Mexico and parts of Asia.

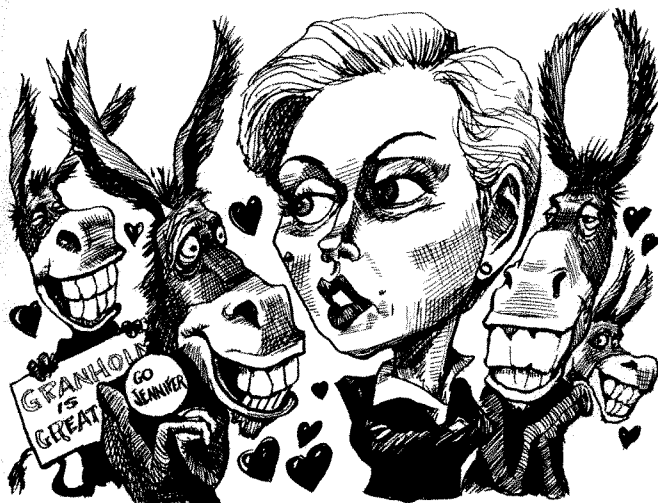
If Arkansas makes cockfighting a felony in November, and if neighbouring Oklahoma (which also has the issue on the ballot) makes it illegal, both states could lose a lot of money. According to the UGBA, raising game fowl is a \$4 billion industry, involving about 300,000 family farmers across the country. That includes people who breed other birds such as pheasants. But the breeders insist that even the cocks are not merely bred for fighting; the feathers are also used for fishing-flies and in Native-American dance rituals. And no doubt a dance ritual is what is going on in that old metal shack down the road?

towers. The judge overseeing the case allowed the families to file the suit while retaining the option to drop it and file for compensation from the fund.

Earlier this month, in a lawsuit seen by some critics as so far-fetched that it is almost recreational in nature, around 1,500 plaintiffs filed a suit against Saddam Hussein, on the basis that the Iraqi dictator supported al-Qaeda. When "terrorist regimes" have been found liable in other cases, the Treasury has had to pay the bills. Congress is sure to close that loophole. But one way or another, the taxpayer will have to cough up. ■

Lexington Jennifer flowers

A woman in Michigan shows there is life left in Clintonism



INCUMBENTS normally have it easy in American politics. The exception this year is the gubernatorial races. With finances in most states in a parlous condition, voters are looking for somebody to blame for the mess. This may be bad news for the Republicans, who have picked up a string of governors' mansions over the past decade. Loyalty to George Bush's stance on Iraq may prop up the odd Republican congressional campaign, but it will not help state politicians. A particularly precarious position to be in is that of a Republican lieutenant-governor trying to get promoted. You tend to get the flak for being part of the ruling administration, without the personal following of your boss.

All these things help explain why life was always going to be tough for Lieutenant-Governor Dick Posthumus, the Republican who is trying to succeed John Engler in Michigan, a swing-state which, according to some locals, is suffering from Engler fatigue. But they do not explain the rise of his Democratic rival, Jennifer Granholm—and the possible problems that candidates like her could spell for the Republican Party.

To hear Democrats talk about it, Ms Granholm is the most exciting thing in Michigan politics since Gerald Ford (well, you know what we mean). Young, clever and telegenic, she currently holds a 12-point lead over Mr Posthumus in the polls. Although she has been the state's attorney-general for a mere four years, Ms Granholm leapt into the national spotlight when she clobbered two veteran bruisers in the Democratic primary—Congressman David Bonior and James Blanchard, Mr Engler's predecessor (and the only Democratic governor in four decades). Ever since then, money has been pouring into her campaign. She has even been endorsed by American Women Presidents, a group that promotes female candidates for the White House (despite the fact that Ms Granholm was born in Canada, which rules her out).

A former beauty queen who graduated from Berkeley and Harvard Law School, Ms Granholm might have been expected to do well in, say, California. Michigan—the home of the United Auto Workers and machine politics—seems an odd place not just for Ms Granholm, but also for her message, a sort of new-age, policy-wonkish pragmatism. She sticks to the centre, making much of fiscal responsibility and the targeting of help to families and small businesses. She also tends to use words like “holistic”.

Her 20-point win in the primaries was built on support from three groups: baby-boomers, women of all stripes and independents. That trio trounced Michigan's traditional Democratic powerhouses, the big trade unions and urban black groups, who both largely backed her opponents.

Centrist politics, charm, even a fondness for new-age jargon: it is hardly surprising that Ms Granholm is being compared to a certain recently retired baby-boomer. Bill Clinton rose to prominence as a reformer who wanted to turn the Democrats from a party of workers to one of consumers, who wanted to talk about softer issues like education and the environment (both Granholm themes), who wanted to bring in women. Last week, the old rogue came to bestow his blessing and lure in more black voters. “I’m getting used to standing around and listening to attractive, blonde-haired women talk,” Mr Clinton joked to 3,000 cheering supporters in Detroit.

The Republicans were only too happy for Mr Clinton to be there—and not just because Ms Granholm, who usually goes to some lengths to play down her looks and gender, probably did not want to be reminded of them yet again. Outside the Detroit rally, protesters held signs with slogans like “Who’s coming next? Ted Kennedy or Gary Condit?”. Mr Clinton’s personal approval-ratings are lower than those of any other living ex-president. Republicans talk about him as a confidence-trickster.

Cunning old Mr Posthumus has tried to depict Ms Granholm as slippery, shallow and more leftish than she appears. “Let’s just say I’ve got different values than come from Hollywood, Berkeley and Harvard,” he says, pointing to his farm upbringing in western Michigan and to his love of hunting and fishing. On Ms Granholm’s plan to “tweak” Proposal A, a 1994 initiative that largely shifted public-school funding from the property tax to the sales tax, Mr Posthumus snipes: “You don’t need a decoder ring to know that means raising taxes.” He is also playing on fears about Ms Granholm’s limited experience. Can somebody who so often uses clichés such as “think outside the box” really be trusted with dour old Michigan’s looming budget deficits?

The diciest issue for Ms Granholm may be abortion. Although she is a committed Catholic, she also supports abortion rights. Earlier this month there was a scene at her local church, with anti-abortion protesters waving gruesome photographs in the faces of parishioners. The Michigan Catholic Conference has also issued an election paper calling abortion “the pre-eminent threat to human dignity”. Michigan’s huge block of independent female voters may have difficulty judging her primarily as Jennifer the feminist attorney-general or Jennifer the Catholic mum.

It's still Bill's backyard

Such questions suggest that the Democrats’ claims that this contest will simply be a re-run of Mr Clinton’s slaughter of Bob Dole are misplaced. Even Ms Granholm’s friends concede that she is not the finished article. But she should still scare the White House—and not just because it does not want a Democrat governor in a swing-state like Michigan. She shows that Clintonism still has a pull—especially among the independents who decide elections. Iraq may be grabbing the national headlines, but on a whole range of economic and social issues, Americans still seem to sympathise with Mr Clinton. They want modern-sounding, non-ideological answers to problems. The man may have taken a battering, but the message still works well, especially when it comes with charm and a touch of glamour. ■



Brazil's presidential election

Lula scents victory at last

SAO PAULO

In a campaign full of surprises, the left-wing front-runner now looks almost unbeatable

BY THIS stage in Brazil's past three presidential elections, with the vote just a fortnight away, Luiz Inacio Lula da Silva of the left-wing Workers' Party (PT) was trailing in the opinion polls, heading for defeat. But in those elections it was the radical, jeans-wearing, trade unionist Lula who was running. Brazilians, more conservative than some of their neighbours, rejected him. This year, Brazil's eternal candidate is a new, centrist Lula in a suit, pledging to run the government's finances sensibly. The makeover is working. This week's polls showed Mr da Silva extending his big lead over Jose Serra, the candidate of President Fernando Henrique Cardoso's centre-right alliance (see chart). Allowing for blank and spoilt ballots, two polls suggest Mr da Silva would get 48% of the valid votes—close to the outright victory needed to avoid a run-off ballot.

In the past two elections, in 1994 and 1998, Mr Cardoso won outright, on the back of his inflation-busting real plan. Mr da Silva has no such big idea to offer. But his moderation and Mr Serra's lack of charisma are encouraging many Brazilians to trust in their desire for a change. Investors would prefer continuity: the real, Brazil's currency, and the country's bonds have slumped in recent months. A \$30 billion IMF loan package announced last month gave some respite. But the markets tumbled again on this week's poll news.

Since much of Brazil's public debt is

tied either to its falling exchange rate or its high interest rates, the debt burden has risen from 53% to 62% of GDP in the past year. If only investors could be convinced that the debt would remain manageable under a Lula government, the real would rise and interest rates fall, thereby lowering the cost of debt service. Otherwise, the debt could become unbearable.

Mr da Silva and his advisers are trying hard to win investors' trust: far from threatening to rip up the IMF accord, as they once would have, they nodded it through. They say they would keep a fiscal surplus, before interest payments, sufficient to stabilise the public debt. And they promise to keep Brazil's system of inflation targeting, though they might loosen its central target by a couple of points.

But Mr da Silva still cannot resist making big spending promises. This week, he pledged to double the value of the minimum wage in four years. Since it determines state pensions and the pension system already has a deficit equal to 4% of GDP, this would be unaffordable without a drastic social-security reform—something Lula's advisers admit will be tough.

The markets would be likely to test a Lula government in its first year, obliging it to keep interest rates high, constraining growth. That might require an even tighter fiscal policy to stave off debt default. But Guido Mantega, Mr da Silva's economic adviser, says the public and the party's

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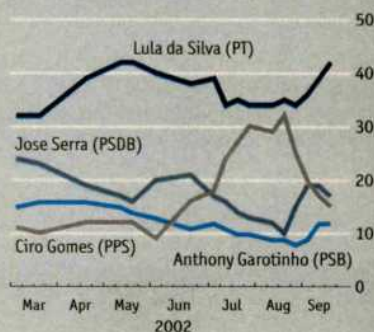
militants understand that its promises cannot be fulfilled at once. He points to Sao Paulo: Marta Suplicy, the city's PT mayor since 2000, inherited big debts, and has ridden out demands for early spending.

Mr da Silva's team recognise the value of trying to reassure investors with early confidence-building measures. Mr Mantega says they would push for immediate approval by Congress of a long-delayed tax reform, even before the new government and legislature take office in January. Another key test would be the choice of finance minister and central-bank governor. The PT has few people with experience of international financial markets. However, investment bankers and officials at multilateral agencies praise Mr da Silva's team for being keen to listen. Intriguingly, Senator Aloizio Mercadante, an economist and one of Mr da Silva's closest aides, recently ran a poll on his website asking if Arminio Fraga, the current central-bank chief who has investors' trust, should stay. A slight majority said yes, at least for a while.

Mr Mantega says that Mr da Silva »

Lula levitates

Opinion poll support for Brazil's presidential candidates, %



Source: Vox Populi

► would continue with Mr Cardoso's public-sector reforms, and some of his infrastructure and social projects. There would be less privatisation. But Mr da Silva would be prepared, for example, to let private firms run water services. The main difference would be a greater willingness to intervene, in matters such as the controversial recent purchase by Petrobras, the state oil firm, of drilling platforms from Singapore. The PT would take into account the broader effects of such decisions on jobs and tax revenues, says Mr Mantega. And it would be more willing to use tariffs and taxes to favour Brazilian industry over foreign producers.

If he wins, Mr da Silva's choices of policy and ministers would also be shaped by the coalition he would have to form to govern. The PT may win only about 80 of the 513 seats in Congress's lower house. Para-

doxically, its most logical partners are Mr Serra's current alliance, of Mr Cardoso's Social Democrats and the catch-all Brazilian Democratic Movement. Many leaders of both parties were alongside Mr da Silva in opposing Brazil's 1964-85 military dictatorship, before moving to the centre.

All sides admit such a marriage of convenience is possible, though it would be difficult: Mr Serra launched fierce attacks against Lula this week, in an effort to ensure a run-off ballot. Mr Serra's supporters insist that a run-off would be a wholly different race. They would hope to pick up votes from defeated candidates by casting doubt on the sincerity of the PT's move to the centre and Mr da Silva's fitness to govern. Maybe. But Mr Serra is not closing the gap and there is only three weeks between the two rounds of voting. Lula has begun to look like Brazil's next president. ■

Human rights in Guatemala

The army on trial

GUATEMALA CITY

A bid to bring the generals to book

IN WHAT looks like a student lecture hall in the concrete bowels of Guatemala's Supreme Court building, lawyers confront each other behind flimsy trestle tables. Despite the simplicity of its surroundings, the trial of three retired army officers which began this month is historic. It is the first time that senior officers have faced justice for crimes committed during a 36-year "dirty war" against left-wing guerrillas that left 200,000 dead, most of them killed by the army.

The officers, a general and two colonels, are accused of ordering the murder in 1990 of Myrna Mack, an anthropologist and human-rights campaigner. She was stabbed 29 times in the street only a few hundred yards from the presidential palace in Guatemala city. In 1993, a soldier in the army's elite presidential-security division (EMP), which functioned as a death squad, was convicted of killing Ms Mack. But he was merely the executioner.

Though the dirty war ended with a 1996 peace deal, and civilian governments had replaced dictatorships a decade before that, the army remains the most powerful political force in Guatemala. So the trial comes as a surprise—all the more so since the three defendants are in prison and have been refused bail. For the first time, the army's order of battle and methods are being revealed in public. This evidence has been pieced together from declassified American documents by Kate Doyle, an analyst at the National Security Archive, an NGO in Washington DC, who has been called as a prosecution witness.

But the trial, which is expected to end this month, is likely to be "an exception rather than the rule", according to Nery Rodenas, the director of the Archbishop of Guatemala's office of human rights. That is because Ms Mack's case has had an extraordinarily tenacious champion in her sister, Hellen Mack, a lawyer who has brought it to international attention.

Those such as Mr Rodenas and Ms Mack, who attempt to investigate the crimes of the past, face threats and violence. Such intimidation has increased since the conviction last year of three officers from the EMP for the murder in 1998 of Bishop Juan Gerardi. The bishop was killed days after he had presented a church report on the dirty war. In May, an accountant at the Rigoberta Menchu Foundation, which pursues prosecutions against former military officers, was killed. A witness ►

Crime in Brazil

Maximum insecurity

SAO PAULO

Getting caught is no problem for Brazil's gangsters

BANGU 1 prison in Rio de Janeiro is supposed to be one of Brazil's most secure. That did not stop its most notorious inmate, Luiz Fernando da Costa (alias "Fernandinho Beira-Mar"), the city's most powerful drug dealer, from obtaining guns and a full set of keys last week, apparently by bribing warders. Mr da Costa and members of his "Red Command" gang then passed through six security gates to the other end of the prison, where they murdered the leader of a rival gang and three henchmen.

The audacity of Brazil's criminal gangs, and the impunity they enjoy even behind bars, is chilling. In July, inmates at a Sao Paulo prison were found to be receiving deliveries of cannabis and pizzas. At another, in January, two prisoners arranged for a hijacked helicopter to collect them from the prison yard.

Prisons and most policing have long been in the hands of state governments. Under a grand anti-crime plan launched by President Fernando Henrique Cardoso in 2000, top-security federal jails were to be built for people like Mr da Costa. But only one has been built, in Amazonia. Disappointingly, public security is not a big issue in next month's presidential election. The main candidates all promise more federal police and tougher sentences. But they seem reluctant to push reforms to modernise the inefficient courts, or to require the states to merge their two rival police forces.

However, insecurity is stirring up races for state governorships. In Sao Paulo, Paulo Maluf, a conservative popu-



Fernandinho's bloody playpen

list, promises harsher prison regimes and "violent" police patrols to repress crime. This week, Geraldo Alckmin, who is seeking re-election as Sao Paulo's governor, fulfilled a pledge to close Carandiru, a squalid and escape-prone jail. But that has meant crowding at other prisons. Mr Alckmin is building new ones; even so, prison numbers are rising faster than new cells. Mr Alckmin also boasts that his police gunned down 12 members of a prison gang which dominates organised crime in Sao Paulo.

Will that be Mr da Costa's fate? He was arrested last year in Colombia, for trading guns for cocaine with the FARC guerrillas. The justice ministry now proposes putting him in a military jail. No thanks, says the defence ministry. Nobody, it seems, will cage this beast.

in the Mack case was flown in from Canada, where he fled after death threats.

The peace accord called for the disbanding of the presidential-security division. President Alfonso Portillo has frequently promised to do so (most recently in July), but this year increased its budget. In practice, it is not Mr Portillo who decides such matters but Efraín Ríos Montt, a former military dictator during the most repressive phase of the war. He is now president of Congress, and the leader of the ruling party. Human-rights groups want him prosecuted for genocide. His supporters want to lift a constitutional ban on dictators standing for president, in time for an election in November 2003. Guatemala's future will depend on which side wins. ■

Colombia's conflicts

Calling up reinforcements

BOGOTÁ

Can new forces of auxiliaries and informers bring greater security?

DURING his campaign for the presidency, Álvaro Uribe made some eye-catching but controversial promises to his war-torn country. He said he would organise a million citizens to support the armed forces, bring in tougher anti-terrorism legislation, and double the numbers of police and professional soldiers. The voters duly gave Mr Uribe a clear mandate to impose authority. Having taken office just six weeks ago, he has lost no time in implementing these plans. Already, human-rights groups are worried. The president, a 50-year-old independent Liberal, is unrepentant. "The policy is not to silence the critics, it's to confront violence," he says. "There'll be no going back."

Colombia's security forces face three main threats: two left-wing guerrilla armies, with a combined strength of perhaps 23,000 fighters; fast-growing rightist paramilitary militias numbering around 10,000, who receive tacit support from some military officers; and the drug trade, which provides finance to the illegal armies. All these forces have profited from the weakness of the democratic state.

Andrés Pastrana, Mr Uribe's predecessor, had begun to strengthen the armed forces: their numbers rose from 117,000 to around 140,000, and those of professional soldiers from 23,000 to 55,000. Thanks in large measure to American military aid, the army now has a large helicopter fleet. Hitherto, the American helicopters have been restricted to action against the drug trade. Now, the United States' Congress has agreed in principle to their use for counter-insurgency. First, however, Co-

lombia has to come up with a formal national security strategy, which will probably happen by the end of the year.

Despite these efforts, the security forces control only about half of the vast country. Of 1,100 municipalities, 180 (some covering thousands of square miles) lack any police or army presence. The new government aims to station units in all of these places within a year, says Martha Lucía Ramírez, the defence minister. That means recruiting 40,000 extra troops by March.

But finance is tight: Colombia's fiscal deficit is climbing (it may reach 4% of GDP this year, up from 3.2% last year). Because of opposition from business, Mr Uribe has scaled back plans for tax increases. On September 16th, trade unions staged a strike against public-spending cuts and planned labour and pension reforms.

To save money, the government has reached back to a 1993 law which allows the army to recruit part-time conscripts as auxiliary police and soldiers. These auxiliaries will account for 15,000 of the new troops. They will be subject to military regulations, but will live in their homes. Human-rights watchdogs fear that they could turn into paramilitary death squads. Another fear is for the safety of the conscripts and their families, since they will lack the protection offered by a barracks or police station. "In the future it is desirable that the army is completely professional," Mrs Ramírez says. "But we know that is difficult in the short term." She argues, too, that locally-resident auxiliaries will enjoy more civilian support in hostilities against the guerrillas than troops or police posted randomly to distant areas of the country.

Another of Mr Uribe's initiatives is also aimed at encouraging civilians to co-operate with the armed forces. In Cesar, Magdalena, and La Guajira, three departments in northern Colombia, police have called

on civilians to volunteer to be informers, passing on information about rebel movements or attacks. The police claim that this scheme has already improved highway security. The idea is to roll out such networks across the country, as part of the target of 1m civilian collaborators. In addition, Mr Uribe has declared Mondays to be "reward days", in which star informants get cash handouts. But even police chiefs acknowledge the danger that informants could be settling local scores or setting traps.

The third prong of the new strategy is tougher laws. Acting under a temporary state of emergency imposed by Mr Uribe after the presidential palace was shelled by guerrillas during his inauguration, on September 10th the government issued decrees that give the security forces wider powers to search and detain suspects, to intercept communications, and to declare war zones in which freedom of movement can be curtailed and foreigners excluded. (This week three Spaniards on tourist visas were expelled, after joining protests linked to the strike.) Mr Uribe is likely to want to make these measures permanent; if so, they could be blocked by the Constitutional Court. Some politicians who support the state of emergency are nervous of sweeping state powers.

The United States, which is expected to offer Colombia \$500m in mainly military aid for 2003, supports Mr Uribe's policies. Human-rights groups do not; they say the army has abused similar powers in the past. They also worry that Luis Camilo Osorio, whom Congress named to the independent post of attorney-general last year, has dropped investigations of abuses by army officers. Mr Uribe insists the emergency measures are not about suppressing human rights: they are about making people observe the law. "We respect controversy," he insists. Just as well. ■



A fistful of pesos for a friendly neighbourhood informer

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The Arab world, Iraq and America

Saddam plays his ace

BEIRUT

And all give thanks for the reprieve, but how long will it last?

IRAQ'S midnight decision to welcome back United Nations weapons inspectors has brought immense relief to the region. The relief is not just over the Iraqis being spared attack, at least temporarily. The collective sigh is also a response to America's new interest in going through the UN, and working with, rather than bypassing, its friends in the region. Given that few expect Iraq's reprieve to last very long, this allows America's strained allies time to prepare for a less abrupt endgame than seemed on the cards a week ago.

The relief, naturally, is keenest among ordinary Iraqis, a few of whom are seen celebrating above. Whatever their quiet wish to be rid of Saddam Hussein, their experience of American arms has not been pleasant. The battered Iraqi dinar, whose price against the dollar is the surest measure of public opinion, leapt 5% on the news of the inspectors' return.

The credit of Arab diplomats also rose sharply. They had been bitterly criticised at home for their failure either to hold back America or to persuade the Iraqi regime to co-operate. Iraq's about-face was particularly gratifying to the Saudis, coming as it did within 24 hours of the kingdom's announcement that it could, after all, contemplate joining American action against Iraq. Similar hints by Jordan and Egypt had left the regime in Baghdad extremely isolated.

The Iraqi government worked hard to put a positive spin on its capitulation. The diplomatic letter announcing its decision was careful to state the hope that renewed

inspections should be a "first step" towards a comprehensive solution that would include a lifting of sanctions. Until now, Iraq had rejected inspections outside the framework of a wider deal. Tariq Aziz, the deputy prime minister, described it as a "courageous, daring decision" that had exposed American belligerence and spoiled its pretext for war. In street interviews, many Iraqis agreed that the move was cleverly timed to embarrass America.

Yet the feeling across much of the Arab world is that this was Iraq's last ace. Mr Hussein may have done well to hold on to it for so long, but the return of inspectors, while delaying the likely onset of war, still leaves his opponents with a pretty full hand. Whether or not the Security Council imposes a stringent new timetable, backed by threat of arms, the renewed inspections will be far more rigorous than in the past.

Americans have been speaking openly of a scenario whereby an "inspections crisis", such as being denied access to a particular site, would help to build the political rationale for an attack. Regional policymakers fear that this will happen soon. Their view is reinforced by the continued build-up of American forces in the region, along with reports that the American tactic for the no-fly zones is to break Iraq's communications infrastructure rather than simply hit air-defence stations.

Interestingly, Iraq showed its awareness of the need to defuse other possible pretexts for war by abruptly dropping a surcharge on oil exports on the same day as

it welcomed the inspectors. For the past two years it has been demanding an under-the-table 15-30 cents per barrel from its customers, as a way of bypassing the tight strictures of the UN's oil-for-food programme. Within a day of Iraq's dual announcements, oil sales surged back after having dwindled, ruinously, to a third of normal levels earlier this month.

But Iraq's fellow-Arabs are bending a receptive ear to America's belated charm offensive. Although the move was overshadowed by news from Iraq, the announcement by the so-called Quartet (America, Russia, the European Union and the UN) of a three-phase plan to resolve the Palestinian-Israeli conflict, seemed aimed at soothing Arab fears that this issue is being ignored. The road map is vague, but it represents a first sign that America might pursue George Bush's commitment last year to the creation of a Palestinian state.

America also proved quick-footed in response to a brewing Israeli-Lebanese water crisis. Lebanon has started diverting water from a spring to dozens of parched villages formerly occupied by Israel. Until now, the spring water had flowed unimpeded into Israel. Bellicose comments by Israeli leaders had raised tensions on this already tense border, where the Hizbullah militia, determinedly hostile to Israel, hold sway. By promptly sending a team of water experts to the area, America showed that it is not in the mood to accept a bust-up that would further inflame Arab opinion.

The pay-off for America's new openness to Arab concerns may come in the form of wider backing for some form of "regime change". Despite deep Arab opposition to an attack on their neighbour, an undercurrent of opinion has begun to see the possibilities of gain. "There could be nothing better than getting rid of Saddam," says Samir Kadi, a Lebanese engineer. "It's just that, until now, America has seemed to want to make enemies of everyone." ■

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Jordan and Iraq

A Big Mac future

AMMAN

Behind the political correctness, Jordanians dream of booty

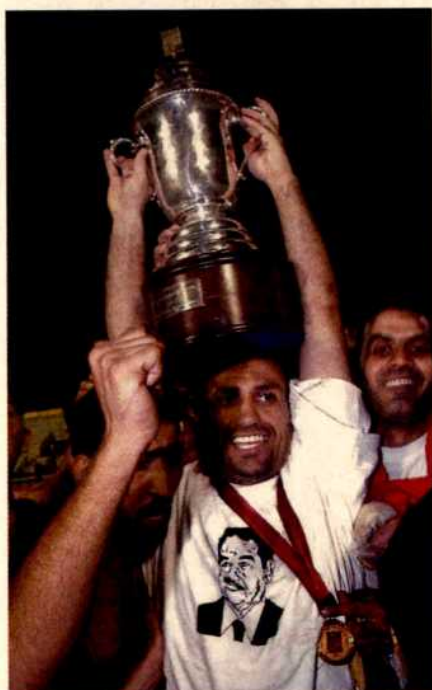
THE ROYAL hotel, built with Iraqi money, towers over Amman, a symbol of Iraq's standing in Jordan. At the opening ceremony earlier this month, King Abdullah himself inaugurated what is by far the tallest building on his capital's skyline. For many Jordanians, Saddam Hussein is the kindly fellow who supplies the bulk of their oil needs for free. And so tied are businessmen to their Iraqi partners, that this week, when Iraq sought to forestall an American strike by allowing the UN's weapon inspectors to return, the Amman stock exchange registered its first major jump in weeks.

Even so, things are not as they were. Earlier this month, Iraqi fans dented the goodwill by spitting insults at King Abdullah during a football match against Jordan in Damascus. Days later, Iraq's visiting vice-president, Taha Yassin Ramadan, appeared to confirm the malaise when, after a meeting with the king, he chose a Jordanian press conference to call on the Arab masses to target American interests in the region once the bombing of Iraq began.

Although barely a day goes by without one Jordanian minister or another denouncing American-British belligerence against Baghdad, the doubters remain. Cafés buzz with talk that Jordan will soon be an American military corridor to Iraq. While ministers insist that the country will not be used as a launchpad in a war, their advisers acknowledge that the United States would probably be able to conduct search and rescue missions, and deploy patriot missiles on the Iraqi border.

The truth is that Jordan has little choice. This summer, America overtook Iraq as the prime market for its goods. Exports to America have soared from \$7m five years ago to \$231m last year, and are set to double this year. King Abdullah has become the most feted Arab leader in Washington.

The press is full of analyses denouncing America's imperialist ambitions. People prophesy doom for the country's tourism, free oil and internal stability if war breaks out. But some officials have begun to relish a future in which Jordan is the chief beneficiary of a pro-American Iraqi regime. Aqaba port, they say, could serve as a prime conduit for rebuilding Iraq; Jordan might receive favoured-trading status with Iraq, displacing Iraq's preferred partners. Some even look to the restoration of Hashemite influence. The vision of Jordan as a miserable sandwich, squeezed be-



He won the cup, but his fans were rude

tween Iraq and America, could come to look more like a Big Mac.

But before they can go for the booty, the Jordanians have to get through a war. It would be a war, said the information minister, Muhammad Adwan, this week, whose effects could be catastrophic. Officials fear that the demonstrations, already planned for once war erupts, could spiral into a fully-fledged East Bank *intifada*. More frightening still, they say, are the intentions of the 350,000 Iraqi nationals already in Jordan, most of them fleeing the burden of sanctions. If only 0.1% of these refugees are Iraqi agents, that would still mean 350 agents. Who knows, asked a Jordanian, what they might be up to?

A measure to raise the cost of an entry visa to nearly 500,000 Iraqi dinars (\$170) looks a bit late. Jordan has declared that, should war erupt, it would seal its borders to prevent more Iraqis flooding across. But the UN Relief and Works Agency, which caters for Palestinian refugees, is already turning its attentions east. Its staff in Jordan have prepared a fleet of 125 vehicles to move an expected build-up at the borders, not just of Iraqis, but Egyptians, Filipinos and Sri Lankan labourers fleeing the fighting. Once the refugees arrive at the frontier, said a UN official, that's it. ■

Iran's constitution

Last chance saloon

TEHRAN

Iran's president in fighting mood

ENOUGH was finally enough for Muhammad Khatami, Iran's reform-minded president. Having become ineffectual to the point that the conservatives started to like him, he is at last having a proper go at the judges who gag and jail his supporters, and at the conservative-dominated Council of Guardians, which, in its capacity as an appointed upper house, summarily vetoes all reformist bills. The president is required to supervise the implementation of the constitution. So far he has been unable to do so.

Time and again, Mr Khatami has drawn attention to constitutional violations, such as the trial without jury of political prisoners, and the council's spiking of legislation. No notice was taken. So legal eagles in his office are now drafting a bill that, at least in theory, will enshrine his right to step in to prevent or reverse violations. And parliament will soon start debating a second bill, also drafted at the president's behest, which seeks to deny the Council of Guardians the right to disqualify candidates from standing for office. Whether or not either bill becomes law, they are already transforming the political landscape.

From the second bill, reformist parliamentarians hope for job security. Extrapolating from the constitution's requirement that the council "supervise" elections, the previous parliament had mandated it to vet candidates for public office. It is an open secret that it intends to disqualify at least 60 reformist deputies from standing for re-election in 2004. The new bill would hand vetting responsibilities partly to the government, and make the process less arbitrary.

For lack of a consensus

After the 1979 Islamic revolution, informal consultation was the norm between the different offices of state, and disputes were settled by the then supreme leader, Ayatollah Ruhollah Khomeini. Now, the executive and parliament are ranged against the judiciary and the country's un-elected institutions—and Khomeini's successor, the conservative-leaning Ayatollah Ali Khamenei, seems unable to impose a consensus. The resulting confusion has made the anomalies in the constitution, and in some laws, all the more glaring.

Mahmud Kashani, a conservative constitutional expert, accuses Mr Khatami of making a bad situation worse. He claims that the bill now being drafted in the presi-

dent's office itself violates the constitutional independence of the executive, legislative and judicial branches. Judges, he says, bow only to more senior judges; if the president were to step in, he could be ignored. Also, or so Mr Kashani says, giving the government a say in vetting candidates is a recipe for conflicts of interest. He expects both bills to be rejected by the council, and "political chaos" to follow.

If either bill is vetoed, Mr Khatami has indicated that the government will draft a bill to hold a referendum on the relevant subject. Assuming, as most do, that Mr Khamenei will himself veto the staging of a referendum, the president's friends say he will resign. A bluff, scoff conservatives, noting Mr Khatami's loyalty to the regime, if not its current form.

Reformists say they take the matter seriously; they recall Mr Khatami's resignation as a minister, on a matter of principle, during a previous government. While everyone feels sure that the election law will be vetoed, some expect the council to appease the president by permitting him his "clarified" power to intervene.

On one thing, all agree; the president's resignation would pave the way for a more authoritarian government. But Muhammad-Ali Abtahi, the president's chef de cabinet, defiantly puts it this way. The bills represent the "regime's last chance". If they do not become law, "society will pitch its tent outside the constitution". ■

Zimbabwe's judges

Cuffed justice

HARARE

Robert Mugabe nobbles judges, too

WHEN a criminal is in charge, judges can expect a rough ride. Literally, in the case of Fergus Blackie, a retired Zimbabwean justice: he was hauled from his home before dawn, held for three nights in jail, and paraded through the bumpy streets of Harare, Zimbabwe's capital, on an open Land Rover, in handcuffs.

On September 16th, Mr Blackie was charged with obstructing the course of justice and, for good measure, with corruption too. The prosecutor alleges that he acted improperly in ordering the release of a woman convicted of embezzlement. But his real crime may be to have sentenced the justice minister, Patrick Chinamasa, to three months in jail for contempt of court, after he ignored two summonses to answer separate contempt charges. Mr Chinamasa never went to jail, as a more obedient judge overturned the sentence, but he was said to have been offended.

Mr Blackie's ordeal may deter other judges from trying to enforce laws that annoy the executive. It was not the first such

warning. Last year, the chief justice, Anthony Gubbay, resigned after receiving death threats. Bearded pro-government militiamen broke into his court shouting: "Kill the judges!". Mr Chinamasa then told Mr Gubbay that the government would not be able to guarantee his safety if he remained in office. Mr Gubbay took the hint.

Since then, six top judges have resigned or retired under pressure from the government. Their colour seems to have been immaterial: black, white, Asian or mixed-race, what they had in common was their refusal to toe the official line. They were replaced with more pliable types. And just in case this was not enough to secure favourable verdicts, the president, Robert Mugabe, appointed three extra judges to the Supreme Court.

The law is his instrument

Mr Mugabe has gone to great lengths to appear law-abiding, in his way. His government has changed the constitution 14 times and passed laws that effectively criminalise peaceful dissent. After two decades of patronage, the police now routinely refuse to enforce court orders the government does not like, or to investigate crimes committed by its supporters. Dissidents who so much as hold an unscheduled meeting are arrested on the spot.

All this is making it hard for the opposition party, the Movement for Democratic Change (MDC), to contest the local elections which are to be held on September 28th and 29th. More than half of the MDC's candidates have dropped out of the race, either because they were afraid of having their faces pushed through closed windows and their genitals jolted with jumbleads, or because such tortures had already been inflicted on them, according to MDC officials. If the ballot were fair, the MDC would romp home, despite its disarray. But even a party as unpopular as the ruling ZANU-PF will have little trouble winning most of the 1,300 seats up for grabs when it is running unopposed in nearly 700 of them.

At the recent summit on sustainable development, Mr Mugabe won loud applause from third-world delegates by promising to right the wrongs of colonialism by grabbing land from white Zimbabwean farmers and giving it to blacks. Back home, his promises are treated with more scepticism, partly because the beneficiaries of his land handout include his wife and most of his inner circle, and partly because his policies have sparked inflation of 135%, unemployment estimated at 70% and an economic contraction forecast to be 11% this year. The independent media who reveal such embarrassing facts are under attack. Another foreign correspondent was ordered out last week, and last month, a bomb incinerated the offices of Zimbabwe's only independent radio station. ■

Ethiopia's divided families

Split by a pointless war

ADDIS ABABA

Despite peace, Ethiopia's border with Eritrea is still closed

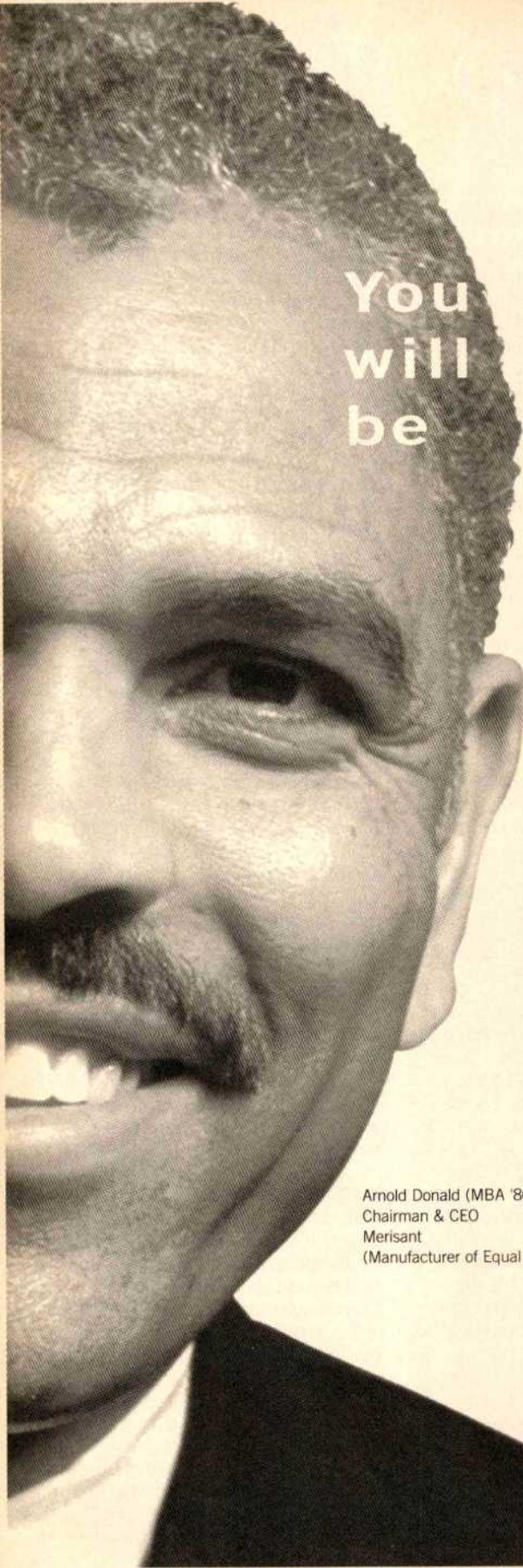
THE war is over, but not for Alemu. He is half-Ethiopian, half-Eritrean, so since the two countries started fighting in 1998, he has found himself unwelcome in both. Before the border became a bone of contention, Alemu's family used to move freely across it. But when the shells began to burst, he was deported from Asmara, Eritrea's capital, on the ground that his father was Ethiopian. When he arrived in Ethiopia, he discovered that his Eritrean mother had been deported to Eritrea.

The shooting stopped in 2000, and an international court ruling settled the border dispute in April. But for those who are still separated, the suffering continues. During the war, an estimated total of 125,000 people were deported from Ethiopia and Eritrea. Many were summarily loaded on to trucks and driven away, leaving their cows and houses behind. Families that were split up cannot easily reunite, because the border remains closed.

Alemu has not seen his mother for four years. He has trouble even exchanging letters with her, because cross-border mail has been blocked. If it were not for the UN, which runs a postal service for divided families, he would not know if she was dead or alive.

Meanwhile, in Ethiopia, he is regularly accused of being a spy, and is nervous enough to ask that his real name not be used. He wants to carry on running the family flour mill, which his mother left behind when she was expelled, but he cannot obtain a licence to do so legally. Nor can he get a telephone or an electricity connection.

Last year, he finally managed to secure an Ethiopian identity card, so he can, in theory, leave town without being arrested. But he often has to bribe police and other officials to leave him alone. Ethiopia's foreign minister described the border ruling in April as a "victory of peace over aggression and violence". The border had barely budged.



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Russia's foreign policy

Vladimir Putin, friend or foe of the West?

MINSK AND MOSCOW

Russia's recent behaviour has made some worry that it is thinking twice about its rapprochement with the West. Probably not so

TO A casual observer a year ago, it looked as if the September 11th attacks had made President Vladimir Putin decide to join the West. To a casual observer now, it might look as if he has changed his mind. Having at first stoutly backed America's war on terror, Russia seems to have shifted recently: it has been cool about an invasion of Iraq, uncomfortably warm towards America's "axis-of-evil" countries, and ever more aggressive towards Georgia, where some Chechen rebels seek refuge.

Last week Mr Putin even threatened to bomb Georgia's Pankisi Gorge—something the Georgians have accused the Russians of doing covertly in the past—because that is where Chechens can hide out. Some Kremlin-watchers believe that, under pressure from Moscow conservatives to stand up for Russia's interests, Mr Putin is demanding a quid pro quo from the gun-slinging George Bush: we'll let you bomb your enemy, if you let us bomb ours.

In reality, though, Mr Putin's critics both at home and abroad are oversimplifying. Neither his original position nor his current one are the knee-jerk reactions they seem. A pragmatist in foreign policy as in everything else, he had started looking for closer ties with America and Europe, and a bigger role for Russia in international bodies, well before September 11th last year. And his support after the attacks did reap rewards. Both the United

States and the European Union awarded Russia "market-economy" status, and the creation of a Russia-NATO council in May marked an about-turn from Russia's previous hostility to the western alliance.

Hardline Russians still complain that Mr Putin has let their country's world position slip—for instance, by allowing American troops into former Soviet Central Asia and by raising too few objections to NATO membership for the three Baltic republics. And in recent weeks Mr Putin did indeed appear to thumb his nose at the Americans. He met the Korean dictator, Kim Jong Il, and there was talk of a \$40-billion trade deal with Iraq and of building five more nuclear reactors in Iran.

But the Russian president and Mr Kim had met before (anyway, Mr Kim meets a lot more people than he used to). And it was the Iraqis that brought up the subject of the deal—and probably exaggerated its size. In any event, staying friendly with such traditional allies is pragmatic and sensible, not just for investment, which will be small, but because Russia could be a mediator that one day helps even such renegades as North Korea to open up.

Meanwhile, Russia's insistence on a UN solution to the Iraq conflict, rather than an American-led invasion, has pragmatic roots too. Permanent membership of the UN Security Council offers one of the few levers of world power that an impover-

ished Russia still has; it would not like to see the Council ignored.

When necessary, the pragmatism also works the other way. For years Belarus's president, Alexander Lukashenka, has wheedled aid and concessions out of Russia while demanding a union of the two countries as a thinly-disguised way for him to become president of all the Russias. But the increasingly dictatorial Mr Lukashenka has no friends in the West. Even his own officials detest him, say foreign diplomats in Minsk. And recently Mr Putin has grown visibly tired of him too.

Last month he responded to Mr Lukashenka's integration proposals by making one of his own: in essence, let the Russian Federation absorb Belarus's seven regions, making the Belarussian president redundant. Earlier this month the Russian and Belarussian press published a transcript of a tapped phone conversation, in which a Russian MP, Boris Nemtsov, told a Belarussian opposition leader, Anatol Lyabedzka, that the Kremlin was sympathetic to moves to undermine Mr Lukashenka. Evidently, Mr Putin does not hold on to traditional allies just for the sake of it.

The situation in Georgia is more worrying. Mr Putin timed his bombing threat to

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coincide both with the anniversary of the terror attacks in America and with President Bush's robust speech to the UN. Russia had often raised the topic of its campaign against Chechen rebels during UN discussions on Iraq. It certainly wanted the world to see the parallel. And American officials concede that their own country's experience of terror has certainly made them more sympathetic to Russia's.

But that does not necessarily mean Russia wanted a deal: a free hand in Georgia in return for giving America a free hand over Iraq. While Mr Bush would probably like to attack Iraq, it is not clear that Mr Putin really wants a full-scale assault on northern Georgia. For one thing, it would be messy. "I don't think the Russian military is capable of clean surgical operations in

Pankisi," says Dmitri Trenin, a defence expert at the Carnegie Endowment for International Peace in Moscow. The posturing may just be Mr Putin's concession to the hawks who think he should be tougher both on Georgia—whose president, Edward Shevardnadze, has enemies in Moscow—and on America.

It may also reflect Mr Putin's own desperation. His harshness against the Chechens first made him popular with voters. But his failure to end the conflict could be a big weakness in the next presidential election, in 2004. He may not, in the end, be pushed to extreme measures, though his latest tactics look thuggish. But rather than simply condemning them, the Americans might be able to help both Russia and Georgia co-operate to find a solution. ■

Macedonia's general election

A hopeful outcome

SKOPJE

Might a new coalition government run fragile Macedonia better?

FOR the western countries which have struggled to hold Macedonia together—by dousing the embers of war between its Slav-Macedonian majority and its aggrieved ethnic-Albanian minority—it was the best election result anybody could have expected.

In comes, as the new prime minister, Branko Crvenkovski, a professed social democrat (ie, ex-communist). Out goes Ljubco Georgievski and his VMRO-DPMNE party, a nationalist movement with roots in the Balkan wars of a century ago. On balance, that was a vote by Macedonia's Slavs for moderation.

But Mr Crvenkovski will have to share power in coalition with a new lot of Albanians. For the party that won most Albanian votes is the equivalent of Northern Ireland's Sinn Féin: in other words, a party dominated by a well-armed guerrilla movement that has been persuaded to renounce violence in return for political acceptance. So the Albanians' Democratic Union for Integration, led by a former guerrilla leader, Ali Ahmeti, is almost sure to share power with the old political bosses of the Slav-Macedonian community who ran the show when Macedonia was part of the Yugoslav federation before its disintegration in the early 1990s.

Western diplomats monitoring Macedonia's politics in the capital, Skopje, are cautiously hopeful. The European Union and NATO, clubs which Macedonia hopes one day to join, were fulsome in praise of the country's politicians and voters.

Sweetness and light, then? Not yet. Both sets of victors remain intensely sus-



Can Crvenkovski make a fist of it?

picious of each other. Only a year ago Albanian rebels had Skopje in range of their mortars. Many Orthodox Slavs, in Macedonia and elsewhere in the Balkans, see them as unreformed terrorists and criminals. Indeed, Macedonia's state prosecutor still has an arrest warrant out for Mr Ahmeti for alleged war crimes committed during last year's fighting. Though the nationalists of VMRO have been ousted at the ballot box, the influence of their supporters in Macedonia's still pervasive criminal underworld remains powerful.

So Mr Crvenkovski needs to start keeping his promises to fight corruption and create jobs pretty fast. Mr Ahmeti, too, will need to rein in his former rebel commanders, still active in the world of smuggling and crime in the region straddling Macedonia and NATO-run Kosovo. Above all, Macedonia's politicians must learn to walk unaided. For Western European countries are getting tired of having to provide so much cash, firepower and high-level attention to the Balkans.

Slovakia's general election

A crucial choice

BRATISLAVA

A choice between the strongman past and the European future

THE general election on September 20th-21st offers Slovaks an epoch-shaping choice. Reject their former strongman, Vladimir Meciar, and they can expect to be invited into NATO later this year and the European Union as early as 2004. After its recent history of shaky democracy and rampant corruption, Slovakia's entry into these western clubs may give new hope to hapless countries further east. Reinstating Mr Meciar, whom the EU has long regarded as beyond the pale, would push Slovakia itself into the hapless zone.

Slovaks rejected Mr Meciar once before, in 1998, when they elected a reform-minded but fractious coalition led by Mikulas Dzurinda. In many ways, this has been a success. Negotiations with the EU have gone well. Though still riddled with corruption, the economy has at least been rescued from Mr Meciar's kleptocracy. Inflation is down and growth is expected to top 4% this year and next.

Still, few Slovaks outside Bratislava, the capital, have felt the improvement. Unemployment is running at 40% in the east, where criminal gangs smuggle migrants and drugs across the Ukrainian border and on into the EU. Health and education remain woeful. In hospitals, patients must bring everything, including lavatory paper. In schools, teachers often demand bribes to mark exams. The government has failed to overhaul the rotten judiciary. Some judges solicit bribes. Not one member of Mr Meciar's government has been brought to justice.

At least Mr Dzurinda has managed to marginalise Mr Meciar, who has done his bit to help. Much-aired television footage of him lunging at a Slovak journalist—fists clenched, face convulsed in momentary fury—inspired editorials suggesting he seek not political office but psychiatric help. His once-solid party has splintered, helping cut his share of support in the opinion polls from 30% to 18%.

Still, his party may yet win more votes than any other. But Mr Meciar is probably too much of a pariah to attract any coalition partners. More likely is another centre-right government team, including Mr Dzurinda's party, an ethnic-Hungarian one, the Christian Democrats, and the populist party, ANO, of Pavol Rusko, who owns Slovakia's biggest television station.

Much will depend on Robert Fico, an ex-communist—a younger, slicker and emotionally more stable version of Mr

► Meciar. He offers an anti-establishment, populist brand of law-and-order rhetoric. His SMER (Direction) party will probably be the only left-leaning one to cross the threshold of 5% of the popular vote needed to gain seats in parliament. If he scores well, he could have enough leverage to become the next prime minister.

That would bring the shady financial backers of his campaign into focus. What they want in return for their money is fuzzy. Many used to back Mr Meciar. Some have energy interests: not for nothing is Mr Fico a backer of nuclear power and eager to reopen energy deals struck by Mr Dzurinda's government. Slovakia, then, would remain out of Mr Meciar's clutches, and thus acceptable to western clubs. But in any event it has a fair way to go before becoming a civilised democracy. ■

Austria's Jörg Haider

A populist bids adieu, for now

VIENNA

The apparent retirement of Jörg Haider could reshape Austria's politics

HE HAS resigned or threatened to resign many times in his political career, only to return in triumph to answer the desperate pleas of his Freedom Party to stay on. But when the 52-year-old demagogue shocked his comrades last weekend by saying he would not seek to regain his party chairmanship, few of the party faithful begged him to change his mind. Indeed, some of his former supporters told him to stop meddling in national politics for good. At least for the time being, it seems that Jörg Haider will no longer play a big part in Austrian politics. That is a remarkable turnaround for a man who, only two-and-a-half years ago, was being pilloried by politicians across the whole of Europe as a threat to western democracy, after his populist Freedom Party had joined the country's ruling coalition.

Earlier this month, Mr Haider had at least had the satisfaction of bringing down that same government after he had virtually forced Susanne Riess-Passer, his party's nominal leader as well as being the country's vice-chancellor, to resign, along with several other Freedom Party people in the government, for being too co-operative with the coalition's senior partner. Wolfgang Schüssel, the outgoing chancellor, who hails from the mainstream conservative People's Party, then called a general election, now due on November 24th.

The Freedom Party's main hope for keeping up its vote at the polls was for Mr Haider to step back into the national fray as party leader and to play on his favour-

ite, well-tested vote-catching themes of xenophobia and hostility to the European Union, especially its policy of embracing new countries to Austria's east.

But this time he had fallen out with too many of his colleagues to let him come smoothly back as party boss. Among other things, they disliked the way he had humiliated the popular Mrs Riess-Passer, who had done much to make the party more respectable. Mr Haider also said he had been threatened by an unnamed "emissary of the military lobby" because of his opposition to the Austrian government's proposed purchase of 18 Eurofighter jets. A man, he said, had walked up to him outside a restaurant and told him, "Don't interfere with the purchase of the jets and keep an eye on your family". Many people found that hard to believe.

In any event, his party is in disarray. Its moderates pleaded in vain with Mrs Riess-Passer to come back as party leader. Instead, Mathias Reichhold, the transport minister in the outgoing government, was chosen as the party's new chairman. An Alpine farmer, he had sided with Mrs Riess-Passer in her struggle with Mr Haider, but his easy-going manner made him just acceptable to the party's radicals, who are now clearly on the defensive.

With Mr Haider out of the picture, Mr Schüssel has a better chance of hanging on as chancellor. If he fails to do so, he will probably bow out of national politics altogether. Many in his People's Party blamed him for teaming up with Mr Haider's lot in the first place, but, with Mr Reichhold in charge, the prospect of the same right-wing coalition might be palatable to a wider range of Austrians. In any event, the Social Democrats under Alfred Gusenbauer say they are confident of making a comeback, perhaps again with Mr Schüssel's lot as their junior partner in coalition. A poll this week put these two main parties neck and neck, with the Social Democrats on 37% to the People's Party's 35%—and the Freedomites down to 12%. ■



Is his Kampf really over?

Sweden's victorious centre-left

On top, as usual

STOCKHOLM

Sweden's winning left is happy to be Western Europe's odd party in

THE Social Democrats, who have run Sweden for 61 of the past 70 years, won their third general election in a row on September 15th and show little sign of losing their grip. Indeed, for the first time since 1968 the government actually increased its share of the vote, achieving nearly 40% against more than 36% four years ago. The incumbent prime minister, Göran Persson, who took charge in 1996, looks set to run the show for quite a while yet.

The Swedish result is all the more striking because centre-left governments are out of fashion in Western Europe. In the past 12 months, voters in France, Portugal, the Netherlands, Norway and Denmark have turfed them out. "We've broken the trend," says Mr Persson, urging his German counterparts to follow suit in their election on September 22nd.

Swedish lessons for Europe? Mr Persson is not a reformer in the mould of, say, Britain's Tony Blair. His Social Democrats have made little effort to distance themselves from the country's still-powerful trade unions. He is broadly against private involvement in public services such as health care. And he has few qualms about raising taxes. Moreover, he fought his election campaign in time-honoured style, repeatedly stressing that it was better to keep up spending on the health service, schools and looking after the old than to cut taxes, even though Sweden's are the highest in the rich world.

For the main opposition party, the conservative Moderates, who promised big tax cuts, the election was a catastrophe. Their vote slumped from 23% last time, in 1998, to a bare 15%. The knives are out for their dreary leader, Bo Lundgren, who failed to convince voters that he could slash taxes yet preserve social benefits.

Many non-socialist voters turned instead to the more welfare-friendly Liberals, who tripled their vote to more than 13%. They had put themselves in the spotlight by suggesting that immigrants seeking citizenship should pass a Swedish-language test. Their leader, Lars Leijonborg, said his party was not anti-immigrant and that racists were "doubly thick in the head" if they voted for it. But Mr Persson accused him, in the absence of any national rivals for the immigrant-bashing vote, of fishing in the "murky waters" of anti-immigrant sentiment. In the south of the country, parties more openly hostile to foreigners made gains in local elections. ►►

► Messrs Blair and Persson are not easy ideological bedfellows but over the next year they will be sharing an agenda as they both try to persuade their compatriots to agree to adopt Europe's single currency, the euro. On that score, Mr Persson's crushing victory should strengthen his chances of doing so, though for a long time he was himself lukewarm towards the idea and must still convince the many sceptics on his party's left of the benefits of ditching the krona.

A referendum could be held as early as the spring, although most expect it next autumn. Opinion polls suggest that most Swedes now want to join. But support for the project has been fickle. Mr Persson has plotted a careful path but obstacles could yet trip him up. Swedes could once again become more hostile to the idea if, for instance, the EU backs a war against Iraq (most Swedes are against), or if the right gains the upper hand in other EU countries, or if more evidence pops up suggesting that EU institutions are corrupt and mismanaged. All such possibilities make many Swedes feel queasy about deeper European integration.

Sweden is keen on enlarging the EU to the east and on pressing for more openness in Union affairs. But, especially if Sweden did decide to join the euro after all, Mr Persson would be reluctant to accept a further reduction in the powers of EU countries that is now under discussion at the constitutional convention in Brussels. The question of Sweden joining NATO may come up in debate in the next few years, as it has done in neighbouring Finland and in the Baltic states. But so far Swedes have shown little enthusiasm for giving up their country's longstanding yen for neutrality.

To ensure a stable majority in parliament Mr Persson will still have to rely on the small Green and ex-communist left parties, which previously backed the government without actually being part of it. Before the election, both had demanded a seat in government as a condition for their continued support. Mr Persson has re-

fused, mainly due to differences over defence and the EU: the smalls are keener on neutrality and suspicious of further integration into Europe. Instead he has offered them "deeper co-operation". Expect him to cut some sort of deal with them before parliament comes back on October 1st. Whatever the outcome, as the left's leader, Gudrun Schyman, jovially puts it: "The red team won". ■

Italy's economy

Is Silvio Berlusconi a liberal?

ROME

Not if his record in government so far is anything to go by

PROMISES, promises. Freeing the economy was Silvio Berlusconi's top priority when his right-wing coalition took office in June last year. If he managed to achieve that aim, many Italians were prepared to overlook his own controversial business past. Mr Berlusconi, a tycoon turned politician, promised to speed up privatisation, overhaul the creaking state pensions system, loosen Italy's rigid labour market, cut taxes, make the government step back and let market forces work their magic. That was the hope.

It has yet to be fulfilled. At the end of August, for example, his government froze the prices of an array of public services—hardly a liberal move. It blocked a rise of less than 2% in the electricity tariff due to take effect on September 1st. No wonder the Refounded Communists, as the unreconstructed bit of Italy's once-Moscow-guided party is known, gave a cheer.

Mr Berlusconi's government is also poised to interfere with energy. It has legislation in hand to annul the independence of Italy's energy regulator, though that would flout the European Union's policy of creating a free market in energy. In banking too, the government has shown an itch to meddle. Earlier this year, on behalf of local councils, it presented a bill that would give it control over a swathe of private charitable foundations with stakes in some big banks.

The irony is that Mr Berlusconi seems to be stemming a tide towards privatisation that preceding left-of-centre governments had encouraged. From 1992 until the beginning of 2001, Italy was one of the keenest countries in the EU to sell off state assets. In that time such sales raised around €113 billion (\$110 billion). Since March last year, Mr Berlusconi has raised just €235m.

One reason is that both central and local governments still have their fingers in many businesses—and they find it hard to let go of the patronage. The Treasury still

owns almost one-third of ENI, a huge energy group, over two-thirds of Enel, a vast electricity company, and 4% of Telecom Italia. Some of Mr Berlusconi's people say it would be foolish to sell now, with the stockmarkets so low. But the political will is plainly lacking as well.

The same timidity makes the government balk at changing Italy's over-generous state pensions scheme. At the end of June, Antonio Fazio, who governs the Bank of Italy, warned that public pensions are becoming unsustainable. They now gobble up nearly 15% of Italy's GDP and 40% of the public sector's current spending. But with the trade unions firmly against labour-market reform, while demanding wage increases to match Italy's inflation rate of 2.4%, the government has simply shied away from tackling pensions.

Despite Mr Berlusconi's reluctance to confront the trade unions, Italy still faces an autumn of labour discontent as contracts are renewed. But he has also managed to upset the employers, who had counted him as one of their own. Previous governments had slightly reduced the tax burden. Mr Berlusconi has so far failed to do so. The chairman of Confindustria, the employers' club, wrote to him this week demanding an urgent meeting to discuss such matters.

To give Mr Berlusconi his due, his room for manoeuvre is tight. Public-sector finances are shaky. The budget deficit will be close to 2% this year and the ratio of public-sector debt to GDP looks set to rise to almost 111%, despite the EU's stability pact, which insists that the figure should go down. Italy's credibility at the European Central Bank in Frankfurt is falling.

The reasons for Italy's poor economic performance under Mr Berlusconi are various. Like other countries, Italy has been hit by the global downturn. For another thing, the second-biggest part of his coalition, the post-fascist National Alliance, likes government control. And other supporters of the government, such as those who emerged from the ranks of the now defunct Christian Democrats, still believe in paternalistic intervention. But another reason may be that Mr Berlusconi has been preoccupied with other issues, particularly his own problems in court.

It was a telling sign of his priorities that one of his personal lawyers, who also chairs the judicial-affairs committee in the lower house of parliament, threatened parliament's dissolution this week. There would have to be a general election, he said, if a bill is not urgently approved that would have the effect of kiboshing the trials in Milan where Mr Berlusconi and a fellow MP in his Forza Italia party are accused of bribing judges. Until the prime minister frees himself from the rigours of the law, do not expect him to set about freeing the economy. ■



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Charlemagne What common foreign policy?

When the going gets rough, Europe's bigger nation-states still go their own way



CRISES have a nasty way of exposing pretensions. On paper at least, the countries of the European Union agreed back in 1993 to share a common foreign policy. For good measure, they decided in 1999, by then 15-strong, to share aspects of defence as well. Many EU countries want to go even further. At a convention on Europe's future now being held in Brussels, the German government, for example, says that a single European diplomatic service should replace national ones: *au revoir* to the Quai d'Orsay; farewell to King Charles Street. Many conventioners want the EU's future foreign policy decided by majority votes among EU governments. Valéry Giscard d'Estaing, the convention's president, wants the Union to have its own foreign minister—and he is viewed in Brussels as fairly cautious, as architects of Europe go. Even Britain's Tony Blair has said that he wants Europe to be a "superpower" (though "not a superstate").

Meanwhile, back on planet earth, an international crisis is in full swing. Europe's three biggest powers—Britain, France and Germany—have distinctly different approaches. Not only do they disagree. For domestic reasons all three countries' leaders positively revel in stressing the distinctiveness of their views.

Tony Blair emphasises Britain's "special relationship" with the United States at every opportunity, carving out a niche as America's most reliable friend and military ally. He knows there are heavy misgivings about war in Britain but equally that any prime minister who allows relations with the United States to be ruptured must pay a high political price. Gerhard Schröder, in the midst of a bitter campaign for re-election as chancellor, has flatly ruled out any military involvement in an attack on Iraq, even one authorised by the UN. In Brussels his men may be urging the EU to run a common foreign policy, but back on the election trail he has suddenly discovered the virtues of a "German way". This has let Jacques Chirac, the French president, present himself at home as the voice of middle-ground good sense. French diplomats tut-tut about Germany's refusal to face up to its global responsibilities, but Mr Chirac has also taken a dig at Mr Blair, casting France as a "true friend" of America, which means it is willing to talk frankly to it, in contrast to "sycophants" (no names mentioned, of course) who blindly agree to everything it proposes.

Where, in all this, are the Union's officials who are meant to

be weaving together the threads of a common foreign and security policy? Javier Solana and Chris Patten, the two voices of any putative joint foreign policy, are in a close-to-impossible position when the major EU powers disagree. Both men flew to New York to attend the UN's General Assembly but over Iraq they are sounding pretty piano. In a big international crisis, Europe's focus has once again switched back to national capitals.

It is not that the EU is incapable of forming foreign policies. It has recently done rather well in the Balkans. Over second-order issues—the International Criminal Court and the Kyoto treaty on global warming—it has developed and promoted policies that differ distinctly from American ones. The gap between European multilateralism and American unilateralism has indeed become a cliché. Even when it comes to Iraq, there are elements of a common European approach—in particular, a strong preference for dealing with the problem through the United Nations. So why do the Europeans look such a shambles?

The reasons are both political and institutional. Paradoxically, given the EU's insistence on taking action through the United Nations, the structures of the UN invite Britain and France to behave first and foremost as nation-states. As a result of the settlement of 1945, they hold two of the five permanent seats in the UN's Security Council. In institutional terms, the European Union simply does not exist at the UN. Advocates of a single European foreign policy have always wanted to replace the French and British seats with a single EU perch on the Security Council. After all, they say, the Union speaks with one voice at the World Trade Organisation: there, as a result, it can look Uncle Sam in the eye. So why not adopt the same formula at the UN? Fine in theory. But persuading the British and French to surrender their inherited rights in such a forum is high-impossible. In any case, attitudes to the use of military force and to the United States still vary widely across the EU. In normal times those differences can be papered over. In a crisis, when countries have to make hard choices, differences are more likely to be exposed.

The European way

Yet despite all this, a European position over Iraq may ultimately emerge by default. Cultural and historical differences have pushed European leaders into taking different positions in the first stages of the crisis. Saddam Hussein's offer to let the UN's weapons inspectors back in may accentuate those differences in the short term. But in the long run almost all EU countries may endorse even an American-led war on Iraq, however vague a UN mandate, and many may chip in with military or logistical help. It is widely expected in Europe that Mr Schröder, if he wins his election, will soften his opposition to America's policy.

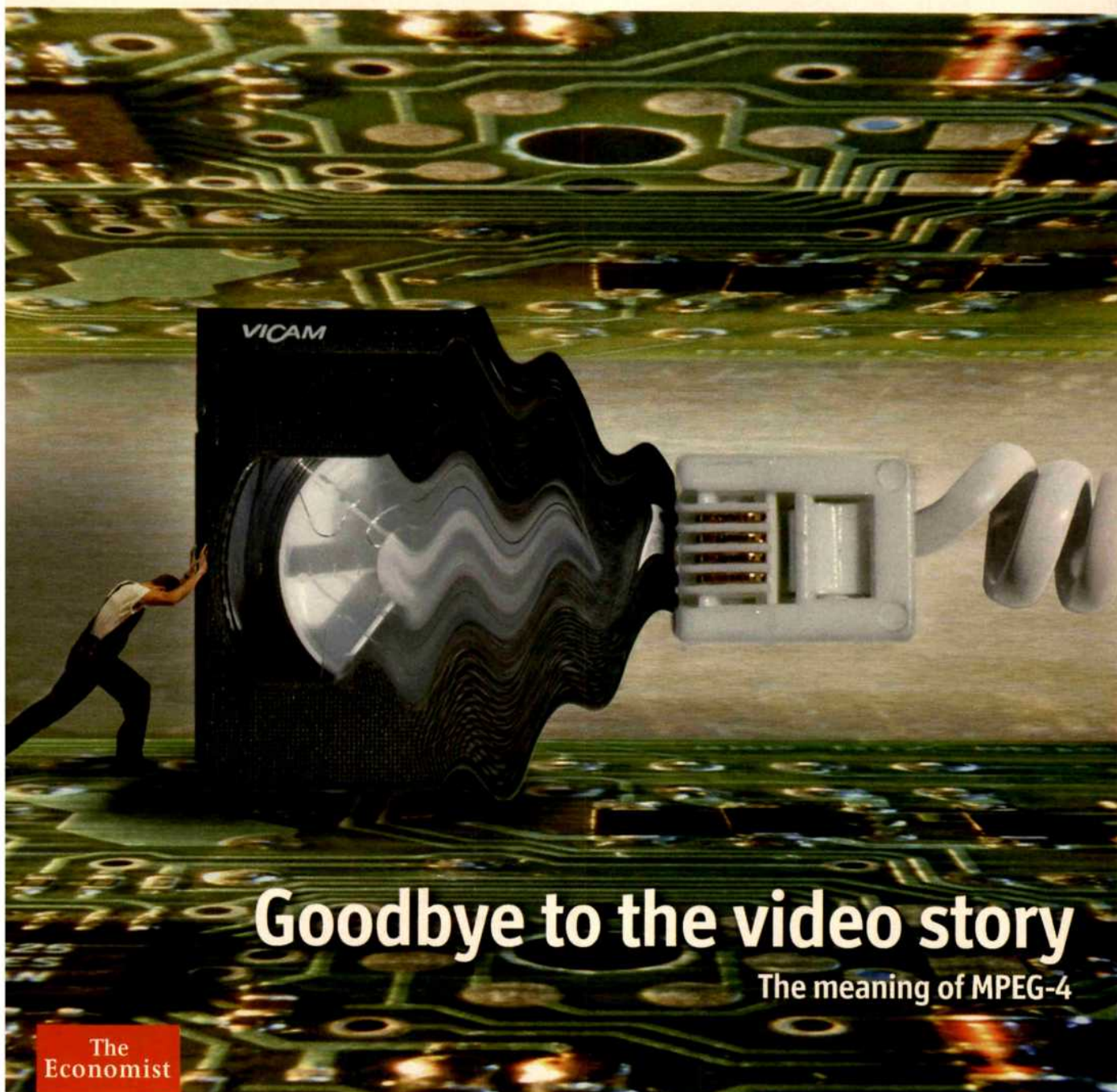
That is because, deep down, most Europeans still harbour a deep fear of the consequences of losing the American security guarantee that saw Western Europe through the cold war. As one of Europe's top policy-makers puts it: "It's appalling that America has put us in this position over Iraq, but in the end we'll have to go along with them because the consequences of a breach with the United States would be even worse."

Over the coming months the Union's leaders may therefore begin to speak the same language again. A belated triumph for a burgeoning new Common Foreign and Security policy? Hardly. More a tactical climb-down in the face of a determined superpower—and conducted at different paces according to the demands of domestic politics. ■

The Economist
Technology Quarterly
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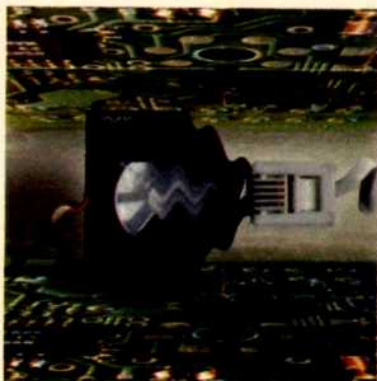
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As the locus of innovation moves on to other fields, can information technology ever regain its pre-eminence?

THE encouraging news, amid all the gloom from the information technology (IT) front, is that innovation continues to thrive. A glance at where, and for what, patents are nowadays being granted suggests that the locus of innovation has begun to move from telecoms, computing and e-commerce towards fresher pastures—especially in genomics and nanotechnology. As this issue of *TQ* was going to press, *The Economist* was praising a group of high-tech innovators for their contributions to the economy at a ceremony in San Francisco. For the judges, the greatest reward was the sheer difficulty of narrowing down the large number of candidates proposed by readers and panellists to a handful of winners (see page 10).

As a pointer to the future, the category receiving the biggest number of nominations was bioscience. Interestingly, more than a few of these could just as easily have been classified under nanotech. Clearly, an intriguing convergence of technologies is under way—as the medical, pharmaceutical and agricultural sectors adopt chip-based techniques.

Meanwhile, contrary to reports of its death, the IT sector proved itself still capable of innovating vigorously—though, understandably, nowhere near as much as during the feeding frenzy prompted by telecoms deregulation, panic over the millennium bug, and the dotcom mania of the late 1990s. The excessive exuberance during the run-up to the millennium has saddled the IT industry worldwide with \$750 billion of debt and some \$250 billion of overcapacity. That is an awfully big hangover for it to overcome.

What, then, are the chances of information technology in general—and Silicon Valley in particular—staging a spectacular recovery? Or has the locus of innovation moved on permanently, creating new centres of technological excellence—such as the strip between San Diego and Los Angeles, where many new genomic ventures are setting up shop?

There are crucial lessons in the way the telecoms industry was deregulated that need to be absorbed before IT can enjoy any serious resurgence. By allowing newcomers to provide high-speed con-

nections over the “last mile” between the incumbent telephone company’s local exchange and the subscriber, deregulation was supposed to usher in all manner of broadband services for the home. Couch potatoes were promised hundreds of video-on-demand channels of entertainment. Online shoppers were going to enjoy better ways of buying things than trudging to the shops. Information addicts would have the pleasure of surfing the web at warp speed.

Six years on, the picture is very different. In terms of the availability of cheap broadband, many consumers are worse off today than they were several years ago. Who is to blame? Certainly, the deregulators failed to ensure a level playing field. And the telephone companies dragged their feet every bit as much as might have been expected when it came to making space available in their local exchanges for newcomers’ equipment. Even so, most of the blame for the collapse of broadband competition must be pinned on the newcomers themselves.

Wrong technology

Few of these “competitive local exchange carriers” (CLECs) and their backers did their homework properly. The DSL (digital subscriber line) technology that most of them adopted was singularly inappropriate for the task. Apart from causing interference problems, the “2B1Q” algorithm used to send broadband digital signals down a pair of copper telephone wires cannot punch its way through the “bridge taps” where local lines are spliced. Making matters worse, few of the CLECs appreciated that shipping data—even though it accounts for more than half of telephone traffic—is a loss-leader. The only things that make money in the telecoms business are voice-based services. The handful of CLECs that understood all this have prospered. The rest have gone out of business, leaving mountains of debt and excess capacity that will take years to mop up.

There are far better ways than 2B1Q for delivering broadband over the last mile. A technology known as TC-PAM has none of the other’s problems and three times its data throughput. Recent variants of this technology do the job better still. Readers with experience of such solutions are encouraged to air their views on our online forum (www.economist.com/forums/tq). With your help, the next issue of *TQ* will try to chart the course of the telecoms recovery. ■



Clean coal's uphill haul

A flurry of activity is reviving clean coal technology. After two decades of unfulfilled promises, will coal come clean this time?

CAN coal ever become a friend of the environment? Coal-fired power stations supply half the electricity used in America (and a similar amount in many other industrial countries) but are responsible for 80% of the power industry's emissions of carbon dioxide—the most worrisome of the so-called “greenhouse gases”. Because of special exemptions, much of the country's coal-derived electricity comes from plants that are more than 30 years old. Many of those plants are approaching the end of their commercial lives, and the thought of having to replace a lot of dirty old power stations with new ones that will have to comply with the Clean Air Act is causing a nightmare in the power industry. Suddenly, energy engineers are talking about “clean coal” technology being on the brink of commercialisation.

That message has been heard before. There was similar excitement over clean coal in the mid-1980s and early 1990s. Large sums of taxpayers' money were handed out to firms developing clean coal. However, the Clean Coal Technology Programme, launched by America's Department of Energy in 1986, has since been criticised by the government's own watchdog body for waste and mismanagement.

The difference this time, say proponents, is that a number of electricity suppliers have started building commercial-

scale facilities that use clean coal. Meanwhile, a handful of companies—including KFX of Denver, Global Energy of Houston, and Air Products and Chemicals of Allentown, Pennsylvania—have pursued ventures to tap the growing interest in clean-coal technology.

Much of the renewed interest stems from the Bush administration's new energy policy, which sees clean coal as one answer to America's energy problem. The new policy has earmarked \$2 billion for invigorating the Clean Coal Technology Programme. Despite its troubles the programme has, over the past 18 years, prompted some 38 clean-coal development efforts. In August 2002, it expanded on those efforts for the first time in eight years, making \$330m of matching funds available for clean-coal projects aimed at curbing emissions of sulphur dioxide, nitrogen oxides and other pollutants, as well as investigating methods for blending coal with other fuels, and for converting it into gas. More tellingly still, a growing number of clean-coal projects are being financed entirely by power companies themselves.

But clean coal means different things to different people. The Clean Coal Technology Programme spans everything from tweaks in power plants to gasification of the coal itself. Simply boosting the efficiency of coal plants—and thus reducing carbon-dioxide emissions—is seen by some as an example of clean-coal technology. Ultimately, however, clean-coal technologies fall into three categories: pre-combustion processing of coal; combustion processes that burn coal more cleanly; and post-combustion processes that scrub the exhausts.

The most widely used clean-coal technologies are post-combustion scrubbers that cleanse exhausts of sulphur dioxide and nitrogen oxides. Scrubbers, which were first introduced in the 1970s, have become cheaper and more effective. A good modern system can remove up to 95% of sulphur from exhausts for a third of the cost of earlier technologies.

Coal treatment and refining processes are getting a lot of attention as well. In the 1970s, the Stanford Research Institute developed a process for transforming western coal—which is high in moisture as well as sulphur—into cleaner-burning feedstock. Belatedly, a Denver-based start-up called KFX is commercialising this process. The company claims that several utilities are now testing its refined coal, called K-fuel. The company's patented process takes western coal and “ages” it at high temperature and pressure to change its chemical composition. The result is a feedstock with up to 60% more heat output per kilogram, far lower mercury, sulphur and ash content, and the potential for far cleaner burning.

Other refining efforts are also being commercialised. Air Products and Chemicals, for example, has plans to bring its process for synthesising methanol from coal-derived gas to market. The biggest stir of all, however, is coming from a new form of generation called "integrated gasification combined cycle" (IGCC). This converts coal into a gas which is then cleansed and burned in a combustion turbine. The advantage of IGCC is that it allows generating companies to capture carbon dioxide from the exhaust more easily, while producing electricity more efficiently than is possible with other clean-coal methods. Best of all, the process can be retrofitted on to existing power plants.

The process involves feeding coal into a gasifier that is injected with steam, oxygen and flux (a compound that creates spots for the chemical reactions to occur). This changes the chemical structure of the coal, producing hydrogen and carbon monoxide in the process. The raw gas is then purified of sulphur compounds, and the tars and heavy oils left over from the restructuring are recycled back into the gasifier for combustion. The clean gas is then used as fuel in a gas turbine to produce power. The attraction is that the turbine's exhaust contains carbon dioxide that is highly concentrated, which makes it easier to capture and convert into something less damaging to the environment.

Even with current designs, Global Energy reckons that IGCC plants will operate at about 40% efficiency, compared with 33% for conventional generation. Future plants are expected to achieve efficiencies of 44% or more. Best of all, the emissions will be well below the Clean Air Act's requirements—with 99% of the sulphur being removed, and emissions of nitrogen oxides, carbon monoxide and particulates (tiny pieces of soot) being far lower than is possible using scrubbers.

So far, two IGCC plants have entered service in America, with support from the Department of Energy. One is Tampa Electric's 250 megawatt plant in Florida, which cost \$300m. The other is Psi Energy's 260 megawatt Wabash River Generating Station at Terre Haute in Indiana, a 1950s power plant that was retrofitted with a gasification process at a cost of \$430m. IGCC plants in the Netherlands and Spain are also helping to prove the technology.

Others are on the way. A subsidiary of Global Energy is building a second plant, with the help of the Department of Energy, in Trapp, Kentucky. It is now moving ahead with plans for a 580 megawatt plant in Lima, Ohio, which will be built at a cost of \$500m without government assistance. Recently, says Stuart Dalton of the Electrical Power Research Institute (EPRI) in San Francisco, a number of

other power companies have enlisted the institute's help on multimillion dollar studies for IGCC plants.

However, two swallows do not constitute spring, cautions Mr Dalton. Indeed, EPRI expects the adoption of IGCC to be modest so long as natural-gas prices remain low. For all their environmental attraction, IGCC and other clean-coal technologies cannot compete economically with natural-gas-fired plants under current pricing and regulatory conditions. Mr Dalton reckons that IGCC only becomes economically competitive when natural gas costs \$4 per million BTUs. Slightly more bullishly, Global Energy reckons that break-even comes at \$3.50 per million BTUs. The average price of gas today is \$2.50 per million BTUs.

But the cost of using dirty fuel is set to rise. California has passed a law restricting emissions of greenhouse gases, and a Senate committee in Washington, DC, has proposed legislation that would tax carbon-dioxide emissions. It is now only a matter of time—probably a few years at most—before power companies in America and elsewhere are faced with the prospect of paying a tax on (or buying tax credits for) the amount of carbon they dump into the atmosphere. Then, say clean-coal enthusiasts, just watch processes such as IGCC take off. ■

Cutting the ties that bind

Better than Bluetooth or WiFi, a robust new wireless scheme promises to deliver multimedia around the office and home without cables or fuss

PERSISTENT protests from America's Department of Defence, Federal Aviation Administration, satellite-radio companies, and firms hawking GPS (global positioning system) equipment have managed to curb the development of ultra-wideband (UWB) wireless technology for more than three years. They all leaned on the Federal Communications Commission (FCC), saying that UWB—which is, among other things, a nifty way of dispensing with the cables connecting home-entertainment gadgets to one another—would interfere with their navigational-guidance systems, radar and satellite transmissions. The big mobile-phone companies even warned the FCC that ultra-wideband transmissions would block telephone calls.

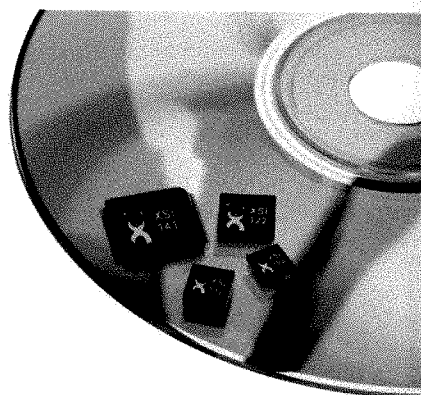
Caught in the middle, a couple of start-up firms trying to build chipsets for

sending and receiving rivers of data using ultra-wideband have responded to each of the new technical hurdles in the hope of being given approval to sell their equipment to the public. Their patience paid off earlier this year, when the FCC at last approved the unlicensed use of the UWB spectrum (3.1 to 10.6 gigahertz).

One of the first to celebrate was Martin Rofheart, co-founder of XtremeSpectrum of Vienna, Virginia. Dr Rofheart has been busy showing off his UWB chipset's performance to consumer-electronics manufacturers from Japan and elsewhere, beaming flawless video and audio between various devices at speeds approaching 100 megabits per second. For applications where more than mere battery power is available, UWB can transmit data at speeds up to 500 megabits per second.

XtremeSpectrum has designed a chipset the size of a business card that electronics firms can incorporate into their own products. The development has proceeded in fits and starts. At one point, the FCC wanted to prevent ultra-wideband from being used in handheld devices. Because of their peripatetic nature, regulators feared that mobile gadgets would interfere with sensitive communications at airports or military installations. But handheld devices such as MP3 players are essential to ultra-wideband's consumer appeal. The technology will allow users to swap thousands of music tracks in seconds instead of minutes or even hours. A compromise was worked out, limiting the frequencies inside which XtremeSpectrum's chipset can operate.

The history of ultra-wideband differs from other wireless schemes, such as Bluetooth and the increasingly popular 802.11 protocol. Bluetooth is a low-power option for transmitting data over short distances at less than one megabit per second, while the 802.11 family offers maximum speeds of either 11 megabits per second or 54 megabits per second. But all three members of the 802.11 family consume too much power and are too expensive for battery-powered devices. In ➤



Chipset for network video

► addition, neither Bluetooth nor the 802.11 family are ideal for handling the vast amounts of data exchanged between digital home-entertainment devices or battery-powered MP3 audio players.

However, both are being promoted by industry groups, and have been making inroads as alternatives to traditional hardwired forms of data transmission. Bluetooth's role is as a replacement for wires connecting computers to their peripherals and mobile phones to laptops. And 802.11b, a variant of the standard that has been given the more user-friendly name WiFi, is becoming popular for wireless computer networks in homes, offices and public spaces.

By contrast, ultra-wideband came out of the defence industry. Its origins go back to the 1950s, when military radar technicians were trying to improve existing equipment. Two decades later, their research led to something called "ultra-wideband synthetic aperture radar". Spy planes and satellites use this kind of radar to see through dense ground cover to locate enemy troops and camouflaged equipment on the ground. It works by showering the target with rapid pulses of broad, low-frequency signals that punch their way through solid objects.

XtremeSpectrum has begun shipping its Trinity chipset to select customers. Dr Rofheart expects Samsung, Sony, Sharp, Panasonic, JVC and other consumer-electronics firms to begin embedding the chipset into DVD players, VCRs, video-game consoles and home-theatre equipment in time for Christmas 2003. Industry watchers predict that the burgeoning home-networking market will reach \$4 billion by 2006. That should leave plenty of room for XtremeSpectrum and its only competitor, Time Domain, which will unveil its own ultra-wideband chipset, called Pulson, later this year.

With their effective broadcasting range limited to only ten metres or so, ultra-wideband chipsets would appear to do what Bluetooth does and more. Apart from linking gadgets together wirelessly, the turf that Bluetooth had staked out for itself includes setting up spontaneous "personal area networks" that allow, say, a smart card in a person's pocket to buy a subway ticket automatically on the way past the barrier. However, with hundreds of times the bandwidth, ultra-wideband has a hefty advantage.

But there could still be room for both. Without the raw speed for swapping video and audio files, Bluetooth would be restricted to the home as a handy wireless-form of "wiring" for low-data-rate connections between computers and their peripherals. Meanwhile, UWB would do the heavy lifting when video and audio needed to move wirelessly around the building. ■

Microchips in the blood

Many of the promised genomic drugs will be impossible to swallow as pills. Instead, they will have to be injected in minute quantities at precise intervals for months at a time. Just the job for an implantable syringe-on-a-chip



No longer a Hollywood fantasy?

SUPPOSE the Human Genome Project turned up lots of superb new medicines—but few of them could be used. Far-fetched? Not by any means. Most of the new drugs likely to come out of research on the human genome will be proteins and other relatively large biological molecules. Such macromolecules tend to be unstable and cannot be delivered orally, because they are easily digested by enzymes in the gut. That is why diabetics have to inject insulin directly into the bloodstream rather than swallow it.

Add an ageing population along with the need for multiple-drug regimens (such as those for Alzheimer's or Parkinson's), and drug delivery becomes a critical issue for the pharmaceutical industry, rather than a mere afterthought. What is needed is a reliable means of delivering multiple drugs in precisely timed and measured doses—without the inconvenience and hazard of injection.

One promising answer lies in an unlikely union of microchips and medicine. The first result of this shotgun marriage is a prototype that exploits methods used for etching silicon computer chips to fabricate small devices that can be implanted in the body, where they can

deliver minute doses of drugs from hundreds of tiny wells in carefully measured quantities. In early animal tests using placebos, this idea—developed at the Massachusetts Institute of Technology—has shown encouraging results.

Now officials at MicroCHIPS, a start-up company in Cambridge, Massachusetts, say they plan to begin tests using actual drug samples in animals this autumn. If the results are positive, pre-clinical trials in people could begin within two years. And if all goes well there, too, the device could be commercially available by 2006. The pay-off for the company could be substantial. The drug-delivery market in America alone is expected to exceed \$22 billion in 2003.

Researchers in this field refer to their goal as intelligent drug delivery. In the case of the MicroCHIPS device, the intelligence is derived from a piece of silicon one centimetre square. Etched in the silicon is a matrix of tiny wells, each designed to hold 150 nanolitres (billionths of a litre) of medicine. The first clinical device will have about 400 wells per chip. Using the same methods of etching and deposition that create the wires and transistors on a computer's microprocessor, the company positions a thin layer of gold on top of each well. An electric current passed through the gold cap at the right moment will cause it to dissolve, liberating the well's contents.

A small onboard processor, packaged with the drug-holding chip, choreographs how each of the 400 wells opens at precisely the right moment over a period of, say, six months. In the case of the MicroCHIPS prototype, the processor is an off-the-shelf model similar to those that power handheld calculators. The whole drug-delivery system finishes up as an implantable device no bigger than a cardiac pacemaker. After being implanted, blood vessels grow around the chip, allowing the medication to diffuse straight into the capillary network.

Timed release of an array of drugs is only the beginning of what intelligent drug delivery promises in the years ahead, says John Santini, president of MicroCHIPS. Others agree that the ability to release drugs within the body in precise amounts at precise intervals will eventually be combined with the ability to measure drug levels (and the body's physiological responses to them) and then to broadcast the information to data-logging equipment outside the patient. When those three functions—drug release, response sensing and data transmission—are combined in an implantable device, physicians will, in effect, have an "intelligent agent" that can work amid the body's own tissues to do their bidding. The start, indeed, of a real-life "Fantastic Voyage". ■

Hanging bytes, pregnant bits

Electronic voting has been getting a lot of attention since the Florida recount debacle. But doing away with a paper-based record may not be such a good idea

WHEN citizens of Palm Beach County in Florida participated in a recent mock election, they were delighted. It was not the patriotic choices (the "Most Famous American" and many other things American) that made them smile, but the new voting-machine—installed to avoid a replay of the recount debacle after the presidential election in 2000. Instead of laboriously punching out chads, voters simply touched a screen.

This new-found voter satisfaction may not survive the real election day on November 5th. Replacing error-prone punch-card voting-machines with touch-screen kiosks, at least in their current form, seems in some ways like jumping from the frying pan to the fire. Most importantly, these direct-recording electronic (DRE) systems raise questions about whether elections should be digitised at all.

At first sight, doing away with paper and letting computers register votes seems an attractive proposition. At least in theory, touch screens should be less confusing than the infamous "butterfly ballots". Computers are unlikely to produce anything like the "hanging" or "pregnant" chads that plagued Florida's 2000 presidential election. Electronic votes can be easily counted and re-counted. At the mock election in Palm Beach, for instance, it took no more than an hour to tally all the votes.

Ironically, it is computer scientists, not officials, who are counselling caution. There is no way to verify that ballots are recorded, transmitted and tabulated properly, argues Rebecca Mercuri, a com-

puter-science professor at Bryn Mawr College near Philadelphia, and the most outspoken critic of DRE. For one thing, vendors have yet to discover the virtues of independent peer review. Worse, it is theoretically impossible to determine whether computer systems are free from programming bugs or nefarious code.

This is why, Dr Mercuri thinks, elections should not be paperless. She would like to see touch-screen systems connected direct to a printer to produce physical evidence of a voter's choice. Such a printout could be inspected by the voter and kept as back-up in case there were problems with the electronic voting system. Without such an external audit trail, votes would be lost forever if a DRE system were to crash.

Although he is best known as the inventor of anonymous digital cash, David Chaum is also convinced that paper, or something like it, still has a role to play in voting. But instead of creating a physical back-up copy of a ballot, the voting system developed by the cryptographer would provide citizens with a receipt with which they could later check whether their vote had been counted.

Such receipts have generally been outlawed because they can lead to vote-selling or coercion. But Dr Chaum proposes a new kind of receipt—one that contains a voter's choice in an encrypted form. A special printer produces a two-layered translucent receipt with the votes in plain text. Once these layers are separated, each shows only a seemingly random pattern of tiny squares, yet contains the encoded vote.

So as not to allow anybody to manipulate an election by tricking the printer, the voter can decide which of the two layers will be shredded by a poll worker and which will be the receipt to take home. The voting-machine keeps an electronic copy of this receipt and later sends it in for counting and posting on the official election website. If voters cannot find their receipt there, it is evidence that there is something wrong with the election.

If this sounds complicated, the tabulating process proposed by Dr Chaum certainly is. The process of decrypting the receipts is split up into several steps, with each step performed by specialised computers called "trustees". By taking samples in a certain way, one can test whether these trustees have changed the votes—without compromising ballot secrecy (which is achieved by deleting the serial numbers from the receipts).

Such receipts, says Dr Chaum, will not only increase voter confidence, but also eliminate the need for trusted voting-machines, such as DRE systems, which are costly because they are based on proprietary technology. In fact, he says, even PCs in libraries and schools could do the

job. The only special-purpose piece of hardware needed would be a small printer capable of printing on both sides of the two-layer receipt.

Yet despite its advantages, it is unlikely that Dr Chaum's approach will be used in an election any time soon—for the same reason that his digital cash has yet to take off. It is ahead of its time and demands too much of users. Even Dr Mercuri's simpler proposal has not made much headway. Adding a paper trail, vendors of DRE systems argue, would defeat the purpose of a touch-screen kiosk.

To overcome such resistance, says Dr Mercuri, the Voting Rights Act, which continues to be debated in Washington, should dictate that all voting-machines have a "physical audit capacity". Yet even sophisticated systems will not improve the reliability of American elections if other problems are not fixed as well. Voter lists remain notoriously unreliable and gerrymandering is rampant. As Bruce Schneier, a noted cryptographer puts it: "There are no technological solutions to social problems." ■

Telling right from left

Many man-made drugs, unlike natural ones, come in right-handed and left-handed versions. Separating them has been a huge problem—but not for much longer

WATCH a small child dressing and it is not immediately obvious which shoe goes on which foot. The problem of fitting molecules into biological systems presents a similar dilemma. In life, and especially in developing pharmaceuticals, shape matters. Using the wrong-shaped molecule to treat a disease is about as effective as using the wrong key to get into your house.

Many chemical compounds exist in two asymmetrical, mirror-image forms—like right and left hands. The molecules, called chiral enantiomers (from the ancient Greek for hand), are chemically identical in most ways. But when they take part in the complex reactions involved in living systems, they frequently have different effects. The differences in activity may be subtle. For example, one form of an odour molecule called limonene smells of lemons, the other of oranges. In other cases, one enantiomer is inert. But it sometimes happens that one form causes serious side-effects. Thalidomide, a morning-sickness drug that turned out to cause terrible damage to

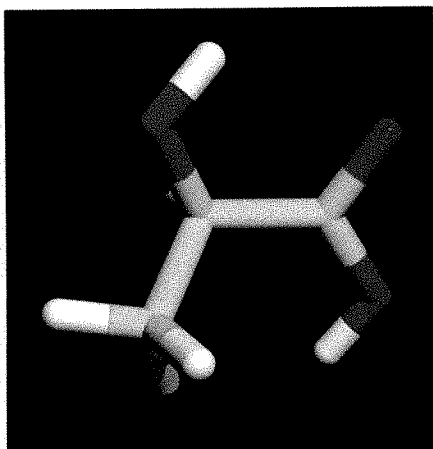
Early and often

Voting-method in US elections, %

	1980	1992	2000
Paper ballots	40.4	21.2	12.5
Lever machines	36.4	25.4	14.7
Punch-card*	19.1	23.5	19.2
Mark-sense*†	0.8	20.1	40.2
Kiosk (DRE)*	0.2	3.7	8.9
Other†	3.0	6.1	4.4

*Electronic tabulation †Optical scanning
†Fax, telephone, Internet

Source: Caltech/MIT Voting Technology Project



Jekyll and Hyde molecule

► unborn children, is widely believed to belong to that category.

Most drugs work by locking into another molecule, often a protein on the surface of a cell, and affecting its function in some way. That is where chirality comes in. Drug molecules with the wrong handedness will not fit the shape of the space they are aimed at. Or, worse, they may fit a differently shaped space on a different target molecule, and thus cause an unintended effect.

Unlike one-handed medicinal compounds isolated from nature—quinine, for example, which is used against malaria—laboratory reactions produce an equal mixture of left- and right-handed molecules. Making pure left-handed or right-handed drugs is therefore hard. And, although the pharmacological significance of chirality was evident in the 1930s, separating the mixtures was until recently too painstaking to be practical. But the effort is worth it. In 2001, single-enantiomer drugs accounted for \$147 billion of sales in America, or 36% of the total drug market, according to Technology Catalysts International (TCI), a consulting firm based in Falls Church, Virginia. Painkillers, antibiotics and antiviral drugs, such as those used to treat HIV, topped the list.

Fermentation is one obvious starting point for making chiral enantiomers, since it is a biological process and its products are therefore likely to be single-handed. But fermentation can deliver only what nature offers—mainly antibiotics. Far and away the most popular route to single-enantiomer drugs is “resolution”—a set of separation techniques that are labour-intensive, wasteful (the undesired product must be discarded or recycled) and inefficient. But they persist, says Sandra Erb, manager of chiral and fine chemicals consulting at TCI, because once a company has registered a drug with the authorities (a process that restricts the ways that the drug may be made to those that are filed with the

application), it takes too much time and money to put other technologies in place.

From the late 1960s onward, William Knowles, Ryoji Noyori, Barry Sharpless and Henri Kagan, among others, began to develop catalysts that made great quantities of single enantiomers very fast. So-called “asymmetric catalysis” won the Nobel chemistry prize in 2001 for Dr Knowles, Dr Noyori and Dr Sharpless. The technology has had an enormous impact on research—and represents a trend away from classical resolution. But it is not yet an important technology in the drug industry because of its use of poisonous heavy metals as catalysts.

There are, however, other ways to get pure enantiomers. Chiral Quest at State University, Pennsylvania, focuses on a single step in the process of making a drug: forcing a chiral product into a left- or right-handed shape with the aid of “toolkits” of ligands—molecules that work with metals to catalyse a variety of reactions. That may prove to be a useful way forward. But in this field, the best answer is probably to go back to nature—or, at least, to snaffle her best ideas.

Natural enzymes, which catalyse the reactions that make life possible, generally turn out only one enantiomer. That is why chirality rules living systems. So

why not simply copy them? ThermoGen of Woodridge, Illinois, does just that. The firm develops biocatalysts for use in making drugs as a complement to other chemical and separation technologies. And Synthron Chiragenics, a drug-discovery company in Monmouth Junction, New Jersey, exploits carbohydrates such as lactose and starch—abundant, freely available and notoriously chiral—as building-blocks for more complex therapeutic drugs.

Dr Sharpless goes even further. People are not very good at making medicines, he says. Life is short, while conventional drug-discovery is a long and uncertain process. So why not put nature, which is much more patient and sophisticated at doing the job, to work directly? Just as a mould can be used to make a copy of a three-dimensional object, Dr Sharpless proposes to use biological targets as templates to guide the formation of their own perfect drugs. He calls the method “click chemistry”, because of the ease with which the molecular building-blocks fit together. He and his colleagues have already used it in the laboratory to identify a molecule that blocks an enzyme related to Alzheimer’s disease. Sometimes the best ideas are also the most obvious. ■

Web of trust

If you like surfing the web, it is probably because you believe people are basically good

WHEN economists try to explain why the Internet is more popular in one country than another, they usually point to factors such as the number of PCs, telephone lines or average years of schooling. But something less quantifiable may be more important: trust. This, at least, is the result of a recent study by Jonathan Leland and his colleagues at IBM, which compared 17 countries.

The Internet’s anonymity and vastness encourage misrepresentation and fraud. Thus, people who are normally suspicious tend to shun the medium, while more trusting souls embrace it. To test this proposition, the team correlated OECD data on Internet adoption with results from the World Values Survey. One question the latter asks is: “Generally speaking, would you say that most people can be trusted, or that you can’t be too careful in dealing with people?”

The statistical link between trust and Internet adoption turns out to be surprisingly strong. The degree of

trust in a society, as measured by the percentage of respondents who answered “yes” to the first part of the question above, explains almost two-thirds of national differences in the percentage of households that have Internet access. Even when controlled for other variables, such as the number of computers, trust remains an important factor.

What to do with such results is less obvious. If governments want people to adopt the Internet, perhaps they should try to increase trust among their citizenry. Of course, there may be other reasons to think this was a good policy. But trust is cultural and historical. Besides, it is not clear what the World Values Survey question actually reveals. And even if it were possible to increase trust, the IBM researchers suggest that high-trust countries such as Norway would benefit much more from such measures than low-trust countries such as Brazil. Trying to narrow the trust divide might only widen the digital divide.

Music to their ears

With compact-disc sales plummeting, record companies are rethinking how to distribute copyright music online. This time, the technology for managing digital rights could actually be smart enough to do the job

HAS the music industry finally got the message? The days of stamping out albums by the million, stacking discs in record shops, greasing the palms of disc-jockeys and then ringing up obscene profits are over. The crude but effective audio compression algorithm called MP3 changed everything. By squeezing audio tracks into a twelfth of their original digital space, a compact disc (CD) "ripped" into MP3 format could be sent over the Internet and downloaded on to someone's computer in minutes instead of hours.

Suddenly, it seemed, more CDs were being freely swapped over the Internet than were being bought. With CD sales slumping—though as much for economic reasons as because of piracy—the record companies are at long last having to learn that there are ways of protecting their copyright material without turning consumers off completely.

Previous attempts to encrypt digital music tracks to prevent endless pristine copies being distributed freely have failed because the protection methods were too easily circumvented, consumers objected to the restrictions placed on their freedom of use, and—perhaps most important of all—nobody wanted to pay for something that they could download over the Internet for nothing. Despite the industry's apparently successful effort to shut down Napster, other file-sharing networks mean that the piracy part of this equation remains as big as ever. But the latest technology for digital-rights management (DRM) is making it possible for content owners to protect music tracks and other forms of copyright material from theft, while offering flexible ways of packaging, distributing and selling entertainment online that are more likely to appeal to consumers.

Not all of the 30m consumers who use pirate services such as KaZaA and Morpheus (two of the bigger content-swapping networks to spring up since Napster's demise) want to steal music and movies. Like shareware, many download tracks on a try-before-you-buy basis. Others turn to pirate networks sim-

ply because they are easier to use. One thing has become clear: if commercial downloading services are to succeed, they must at least match the virtual jukebox features and content libraries that the illegal services provide.

On cue, RealNetworks, Microsoft, IBM and America Online have started offering far better encryption tools for their popular video and audio players, making them less of a nuisance to use. Using DRM, copyright owners still have to encrypt content such as songs and movies. And to play those encrypted files, a user still has to buy a licence that includes a code or digital key to unlock the content.

So far, no different. But the technology now allows record companies, film studios, artists and publishers to vary the rules that control how their content is used. And that, in turn, is letting record companies and other content owners experiment with more profitable ways of doing business.

For example, subscribers to some commercial online-music services are now given the option to send encrypted copies of songs to friends. In exchange for the key to unlock the content, record labels can choose to charge or give the song away free if the friend provides, say, demographic details about himself.

Another example of DRM in use is Arista's recently launched web channel for fans of the band Boyz II Men. The channel serves up unreleased tracks, early access to concert tickets, exclusive videos, lyrics and singing lessons from members of the band for an annual sub-

scription of \$25-35. Meanwhile, film studios are using DRM to secure content for test screenings of films, allowing them to be distributed without the risk that copies might "leak".

On top of that, Microsoft, Nokia, IBM, Intel and others are working on hardware-based encryption technology, which is more difficult to hack into than today's software. Michael Aldridge, a product manager at Microsoft, expects to see encryption chips embedded in portable devices such as DVD players with Internet access and mobile phones, as well as PCs and set-top boxes. Such tools are helping to persuade content owners to overcome some of their suspicions about the Internet as a distribution channel.

Some have been persuaded already. Pressplay, a joint venture between Sony and Universal, has expanded its catalogue to 100,000 tracks—a big improvement over earlier offerings, though still a fraction of what is available on pirate services. By applying new rules for content access based on Microsoft's DRM software, Pressplay has been able to add features that consumers demanded. Until recently, people could rent songs only for a limited period. For \$9.95 a month, they can now get unlimited downloads, save tracks permanently (for an additional 99 cents a song) on a PC's hard-drive, transfer files to portable devices, and even "burn" CDs (ie, store tracks on recordable compact discs)—an idea that was once anathema to record companies.

Other content owners are being more adventurous still. Record labels such as Virgin, Arista and Sony have begun to cross-promote CDs with online fan clubs. Some of them have started to incorporate special passwords into CDs, to give fans access to artists' dedicated websites. By using DRM tools to protect the content of such sites, the record companies can do clever tricks. For instance, the passwords may include a unique identifier that can be used to capture basic information about customers. This can then be used for cross-marketing—ie, offering consumers something that others with similar tastes have also bought.

Inevitably, embracing online distribution of copyright material involves some risks. That is something that many of the media giants—which have traditionally relied on money-spinning record labels to underwrite costlier movie and television ventures—are reluctant to accept. But at least they now have a better set of software tools to protect their copyright. More to the point, they now have the chance of a whole new way of doing business. That could encourage ideas which are more adventurous—and profitable—than trying fruitlessly to stuff armfuls of music albums into the limited rack-space at record shops. ■



Song swapper shows the way

Thanksgiving for innovation

Governments worship at the altar of innovation for good reason: it now accounts for more than half of economic growth. In recognition, *The Economist* has inaugurated a series of Innovation Awards

SINCE its beginnings in the early 1840s, *The Economist* has been continually intrigued by entrepreneurs, and especially by their remarkable knack of being able to conjure up wealth, seemingly from nothing. At the same time, the paper has been constantly frustrated by the inability of economics to explain in detail how the wealth-creation process works—and why it has been so extraordinarily difficult to forecast economic growth.

The basics are simple enough. The output of an economy depends on its inputs—simplifying a bit, capital and labour. But it is not just a matter of doubling the inputs to get twice the output. There are embarrassing quirks such as scarcity and the law of diminishing returns to deal with. Therefore, over the years, the theory of growth has incorporated a rider to explain why adding more and more capital to a given workforce, or an increasing number of workers to a fixed amount of capital, results in successively smaller increases in output.

So far, so good. But how, then, do you explain why returns on investment in rich countries were considerably higher in the second half of the 20th century than during the first half? Why, for that matter, has the gap between the rich and the poor parts of the world been widening rather than narrowing? Economics teaches that, when the stock of capital is rising faster than the workforce—as has demonstrably been the case in industrial countries since the second world war—the return of each additional unit of capital should fall over time. But instead of declining, it has been rising in America, Europe and Japan. Something was clearly happening beyond mere capital accumulation and the fine-tuning of aggregate demand by tinkering with public spending, tax rates and the supply of money.

For want of a better explanation, the missing factor in the growth equation is often thought to be the addition of new knowledge gleaned from scientific discovery and technological progress—in short, innovation. In this scheme of

things, innovation accounts for any growth that cannot be explained by increases in capital and labour. And though the return on investment may decline as capital is added to the economy, any deceleration in growth is more than offset by the leveraging effects of innovation. That explains why rates of return have stayed high in rich countries, and why poorer countries have not caught up.

Governments worship at the altar of innovation these days for good reason. Far from being simply some missing factor in the growth equation, innovation is now recognised as the single most important ingredient in any modern economy—accounting for more than half of economic growth in America and Britain. In short, it is innovation—more than the application of capital or labour—that makes the world go round. And, so, after almost 160 years of puzzling over such matters, *The Economist* has decided that the innovators of the world are due some special recognition.

It is not possible to recognise all the countless innovations that have helped to spread wealth, health and human happiness around the world. But with the help of suggestions from readers and a panel of independent experts, our judges (see box) have chosen a handful of people who have made the biggest contribution to the wealth-creation process in their own fields over the past few years. As we went to press, the winners were being announced at *The Economist* Innovation Summit and Awards in San Francisco on September 18th. Henceforth, the event will be an annual affair—and one that we hope will become a fixture in the calendars of innovators everywhere.

We divided the technological spectrum into five broad bands—bioscience, computing, energy/environment, nanotechnology and telecoms—and, with difficulty, selected this year's winner for each category. But there were some serial innovators who could not be classified. So, late in the day, we added a sixth "no boundaries" category and selected a winner there, too. Here, then, are the innovations, and the individuals behind them, that we are honouring in 2002.

Bioscience

Leroy Hood, director of the Institute for Systems Biology, University of Washington. Dr Hood, a geneticist, immunologist and biotechnologist, was a driving force behind the successful sequencing of the human genome in the 1990s. Without the

automated DNA fluorescence sequencer developed in his laboratory, completing the Human Genome Project could have taken the best part of a century. Dr Hood also had a hand in turning the project into a race. He was a co-author, in 1996, of a paper called "A New Strategy for Genome Sequencing". This described a new way of assembling short DNA sequences ►►

The judges

Ronald Cape, co-founder and final chief executive, Cetus Corporation (now part of Chiron Corporation), Emeryville, California.

David Farber, professor of telecommunication systems, School of Engineering and Applied Science, and professor of business and public policy, the Wharton School, University of Pennsylvania, Philadelphia.

François Grey, professor of nanotechnology, Technical University of Denmark, Copenhagen.

Vinod Khosla, general partner, Kleiner Perkins Caufield & Byers, Menlo Park, California.

Mark Levin, chairman and chief executive, Millennium Pharmaceuticals Inc, Cambridge, Massachusetts.

Amory Lovins, chief executive, Rocky Mountain Institute, Snowmass, Colorado.

Andrew Odlyzko, director, Digital Technology Centre, and professor of mathematics, University of Minnesota, Minneapolis.

Larry Page, co-founder and president of products, Google Inc, Mountain View, California.

Ian Ritchie, principal, Coppertop, Lasswade, Scotland.

Paul Romer, professor of economics, Stanford University, Palo Alto, California.

Paul Saffo (co-chairman), director, Institute for the Future, Menlo Park, California.

John Eckhouse, editorial director, Phocas Partners, Oakland, California.

Charles Pelton, general manager, Phocas Partners, Oakland, California.

Ludwig Siegle, technology correspondent, *The Economist*.

Nicholas Valéry (co-chairman), editor, *The Economist Technology Quarterly*.



Goodbye to the video store

Streaming video: For too long, "video-on-demand" has promised more than it could deliver. But new ways are emerging for shrink-wrapping massive video files for delivery over the Internet

IT SOUNDS like the movie addict's ultimate fantasy: a TV-mounted set-top box that taps the film libraries of Hollywood's big studios. A film buff could peruse thousands of titles spanning dozens of genres, from enduring classics to the latest blockbuster releases. After deciding what to watch, viewers would enter a password, confirm credit-card details, then sit back as 5.1-channel surround-sound video streams from a remote web server into a home-theatre system in their living room.

Too good to be true? For the moment, yes. Bespoke video-on-demand is at least three years away. But the difference now is that Movielink—a recently formed joint venture between MGM, Paramount,

Sony, Universal and Warner Bros—is preparing a collective library for just such a service. The venture intends to serve up an almost unlimited selection of films over the Internet—and, eventually, through a web-connected set-top box.

There is only one problem: the current scheme for converting an average two-hour epic into a digital file results in about five gigabytes of data—equivalent to five billion letters of the alphabet (ie, close to a billion words in English). With each byte comprising eight binary digits (or "bits"), a typical movie contains no less than 40 billion bits of data. Trying to stuff that many zeros and ones through the copper lines that link most homes to the Internet—even via a broadband DSL (digital subscriber line) or cable modem connection—would take all day. If there is ever going to be a profitable online video service, content creators in Hollywood and elsewhere must figure out how to squeeze those hefty film files through narrow digital pipelines.

That is where "codecs" (compression/decompression algorithms) come in. These are sophisticated, and often propri-

etary, mathematical formulae that can quickly scrunch hours of digital video and determine where best to make nips and tucks unnoticeable to a viewer. The end result is a compact digital file.

One of the most prevalent codecs is MPEG-2. Established by the Moving Picture Experts Group in 1994 as a standard for digital television, MPEG-2 governs DVDs, satellite TV and digital cable content. This requires a minimum transmission rate of two megabits per second for video scenes with little movement in them and up to 80 megabits per second for action scenes, so there is little hope of sending MPEG-2 video to homes using even the fastest of Internet connections available today—which, at best, barely break the one megabit per second barrier.

More muscle needed

Yet, if the future is indeed "anytime anywhere" video-on-demand, as digital-media buffs suggest, then Movielink, Intertainer and other online film sites will require a codec with many times the compression muscle of MPEG-2. The demand for such a codec is spurring a feverish race ▶▶

"The consumer-electronics makers cannot afford to lose the battle for the set-top box."

- ▶ between developers all angling to create the *de facto* compression/decompression standard for online video delivery.

There are the established organisations, such as RealNetworks, Microsoft and Apple, each with a video-playing software product (ie, "media player") that exploits the firm's own proprietary codec. With 29m users, RealNetworks hopes to propagate its popular RealPlayer beyond the desktop and into set-top boxes, cell phones, PDAs (personal digital assistants), and anywhere it imagines full-motion video might be feasible. Microsoft is closing in on RealNetworks with its Windows Media Player that is now reckoned to be on some 13m personal computers. Apple's QuickTime comes third with 8m users.

It is the upstarts, however, who are better positioned to rule the future of video-on-demand. For instance, the latest iteration of the Moving Picture Expert Group's standard, MPEG-4, is honed to function smoothly on consumer-electronics devices, which gives it an advantage over Microsoft, RealNetworks and Apple, whose algorithms are better suited for the beefier microprocessors inside desktop PCs. And there are a handful of others, including Pulsent, On2, and DivXNetworks, each hawking their own video codecs to content creators and electronics manufacturers, convinced that their technology is the best for the job.

Ryan Jones, who tracks media and entertainment strategies for the Yankee Group, a consultancy based in Boston, believes that Microsoft and RealNetworks will lead the way on the PC, mainly because they have reliable systems for stemming piracy. But gathering around the computer in the study to view the latest Star Wars sequel is unrealistic. "Consumers want the movie experience in their living room," Mr Jones insists. That is exactly what those developing the newest video codecs are counting on. Mr Jones believes that the first step will be the evolution of the set-top box—the device that decodes the cable or satellite feed for displaying on TV—into a competitive consumer-electronics product.

Such a trend will turn the movie, video and TV businesses upside down. Currently, the design of set-top boxes is largely in the hands of the cable-TV operators, who want to control the kind of content accessible over their networks, such as pay-per-view (they choose the movie, you choose the time). Eventually, however, the cable providers will find

themselves ceding control over the set-top box to consumer-electronics manufacturers such as Matsushita, Sony and Philips, on the one hand, and to content creators, on the other. Why? Because both the technological and market forces will simply overwhelm them. As a result, the set-top box will handle video-on-demand from any number of providers. Users will then access the content they wish to see using an Internet-like "browser" displayed on their TV screens. Eventually, film studios will rent or sell new films direct to the public.

The implications of such a trend: declining influence of the movie-distribution chains that hold sway over when and where new films are released; few video stores outside large urban areas; and dwindling attendances at cinemas everywhere. Cable providers will get their cut in the form of payment for opening their networks to third-party content.

Meanwhile, the set-top box will replace the VCR—the greatest single product the consumer-electronics industry ever produced, and one which, at its peak, generated half the industry's sales and three-quarters of its profits. That is why the consumer-electronics makers cannot afford to lose the battle for the set-top box.

One codec or many?

For codec makers, the aim will be to become the standard means for compressing all those thousands of movies that will be streamed into millions of homes. Doing so could make one company (or, in the case of MPEG-4, one consortium of patent holders) very wealthy.

Today, it is still not clear whether a single codec will emerge as the prevailing standard—just as MP3 reigns over the audio world. Nor is it yet clear whether future set-top boxes will become more like a PC, with their own microprocessors and built-in software to juggle multiple codecs. The answer could come when some media mogul—say, Jim Ramo, the boss of Movielink—chooses a single codec to compress all his company's content. That would oblige set-top-box makers to build compatible devices, rendering all other codecs instantly obsolete.

In the meantime, few are hanging around for that day to arrive. Instead, codec firms, envisaging an imminent gold rush, are spending millions promoting themselves to content providers and electronics companies. These, in turn, are hoping to avoid the blunders made by the music industry when it failed to embrace

the money-spinning potential of MP3 until it was too late.

At the moment, MPEG-4 has a head start in the race to become the prevailing codec for streaming digital video. In essence, MPEG-4 is a set of technical specifications that define a patented process for compressing and decompressing video. Because nearly 90% of Internet users connect over a dial-up line, the previous version of the codec, MPEG-2, would quickly clog the pipes. MPEG-4 tackles this problem by slashing the bandwidth requirements to as little as 40 kilobits per second—some 50 times leaner than MPEG-2—while preserving clarity. At higher bit rates, MPEG-4 manages near-DVD quality.

The trick MPEG-4 uses to render crisp video without hogging bandwidth is a process known as "object-based compression". Previous MPEG schemes simply divided each video frame into a grid, then tagged each block with a unique data signature. MPEG-4 begins with this strategy but takes compression a step further. Instead of capturing the sum total of each frame, MPEG-4 considers separate regions within the picture and decides how to handle them on the fly. For example, if the background between two consecutive frames remains unchanged, while the foreground varies, MPEG-4 will compress the static background and treat the image as a still picture. As MPEG-4 streams video over a network, static backgrounds are sent once, reserving bandwidth for dynamic parts, which have to be compressed and retransmitted as they shift positions.

Overall, MPEG-4 incorporates 23 different mathematical profiles. These enable users to adapt its algorithms to operate on a variety of devices, including pocket PCs and set-top boxes. Despite that, Mr Jones reckons that other, newer codecs could win the battle to rule the set-top box. The reason is MPEG-4's tough licensing terms. Anybody wanting to integrate MPEG-4 into a particular video streaming device must pay stiff royalties to a group of 23 companies, which together own several hundred related patents.

Between them, the consortium members have established an independent licensing body called MPEG LA to hammer out royalty agreements between MPEG-4's patent holders and the companies hoping to use the codec. Larry Horn, vice-president of licensing and business development at MPEG LA, explains that the licence is non-exclusive, giving any ▶

"Others are counting on MPEG LA's licensing rules to steer content creators towards other codecs."

firm the right to negotiate a royalty deal.

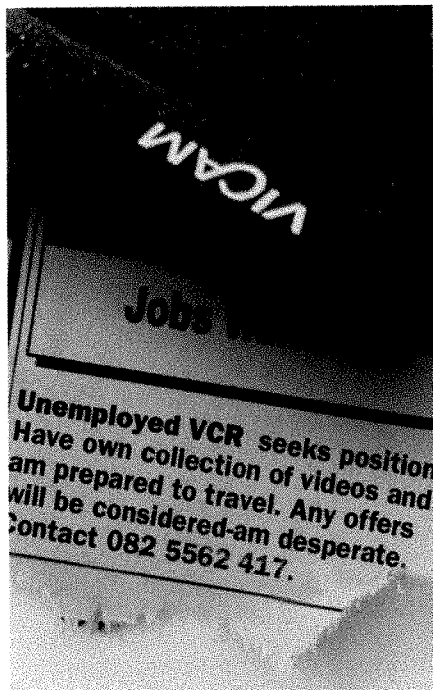
The terms of those agreements, however, are still up in the air. Initially, MPEG LA introduced a scheme that would require companies employing MPEG-4 in their technology to pay a 25 cents royalty for every machine with a copy of the codec incorporated, plus a "per use" fee of two cents an hour. In other words, if a viewer watched a video encoded in MPEG-4 from CNN's website, the news network would have to pay patent holders a royalty. Although the proposed amounts were small, MPEG LA made no allowance for differing content types, free or otherwise. If, for example, tens of millions of people suddenly began downloading a two-minute video clip of the World Trade Centre collapse, the ensuing royalties would bankrupt CNN within days.

Following an uproar from the industry, MPEG LA reworked its royalty arrangements. In July 2002, Mr Horn announced a modified structure that places annual caps on certain types of content usage. Other features include an option for media firms and electronics manufacturers to pay a one-time licensing fee, a per-subscriber charge, or a pay-by-the-minute rate. The last would value a downloaded copy of "Black Hawk Down" at about five cents.

Too little, too late?

Many in the industry believe that MPEG LA's final licensing terms could still suffocate innovation. Apple was forced to delay the release of the latest version of its QuickTime player (version 6.0), which incorporates MPEG-4. Initially, it declared the licensing terms too onerous. Apple relented once MPEG LA revised its terms. Douglas McIntyre, head of On2 Technologies, a software company based in New York that has developed a codec called VP5, has been one of the most vocal critics. His company recently posted a tome online, criticising MPEG LA's strategy point by point. "It is a move by a few very large companies to dominate a market and fix prices," says On2.

Mr McIntyre and others are counting on MPEG LA's draconian licensing rules to steer content creators and electronics firms towards an array of other video codecs. Anybody in the business of using video compression is bound to consider MPEG-4 as well as codecs from RealNetworks, Microsoft and Apple, admits Mr McIntyre. But he points out that other codecs work as well, if not better, and come



with fewer licensing strings attached.

On2's own VP5 technology is one of several emerging codecs that provide potential users with a serious alternative. Streaming at 400 kilobits per second, about half the speed of a DSL connection, VP5-encoded video looks almost as good as images from a DVD. The company guards its compression technique jealously, but Mr McIntyre attributes most of the work to pre- and post-processing tools. These are methods for manipulating digital files before the video is compressed and after it is decoded. To that end, VP5 scrutinises data rates, making on-the-fly adjustments to image softness, colour tone, and pixel size. But with debts of more than \$100m, On2 has been seeking new partners. It recently announced a deal to use its codec in chips for set-top boxes and mobile telephones produced by Texas Instruments.

Then there is Jordan Greenhall, a former executive of MP3.com, who amassed a wealth of experience as a broker of "content deals" for that renowned audio portal. Mr Greenhall now heads DivxNetworks of San Diego, California, which is marketing a video codec that aims to reproduce the experience of being in a cinema. Divx began as a cult movement when Jérôme Rota, a computing and digital-video guru, wrote the codec in 1999 to help him crunch graphics. Word spread, and soon Divx video appeared Napster-

like on file-sharing networks around the world. So far, more than 12m copies of Divx have been downloaded, and thousands of (mostly pirated) full-length feature films, television shows, music videos, and pornographic movies are circulating the Internet encoded in this popular format.

DivxNetworks, founded recently by Mr Rota and Mr Greenhall to take advantage of the codec's grassroots success, has raised \$11.6m in these difficult times for venture capital. Its latest codec, Divx 5.0, is said to be particularly good at preventing "tearing", a playback error that occurs when the software cannot "render" the video for display at the same pace that it is being decompressed and fed into the media player. The overload appears as a frayed line across the middle of the frame. Similar to VP5, Divx 5.0 massages the decompressed video to prevent tearing, dropped frames and other glitches.

Objects beat blocks

One of the newest video-compression tools comes from Pulsent, a Silicon Valley start-up that has toiled for the past four years in self-imposed secrecy. The company claims that its "stealth team of scientists" is developing a codec that breaks the 20-year paradigm of "block-based" compression techniques. Pulsent's chief executive, Adityo Prakesh, is cagey about the specifics. But his company is not without cash, having raised \$33.5m from private investors.

According to Mr Prakesh, the Pulsent codec identifies objects on the screen as unique entities. Whereas block-based compression and object-oriented codecs slice up backgrounds and foregrounds into grids, the Pulsent approach actually pinpoints real-world items in the frame—such as a person, tree or building—and processes each element separately to optimise the playback's performance. Mr Prakesh believes that his firm's codec will revolutionise video compression—so much so that he is pumping money into the development of a chip that can encode and decode files in real-time using the Pulsent algorithms. The aim is to get the chip into set-top boxes for video-on-demand services.

It is difficult to verify Pulsent's claims. Experts and rivals are curious but tentative. It is still too early to know which codecs will endure. At this stage, the strategy for most is to get their product into the marketplace and build their brand. That is not the case with Emmett Plant, a 25-year- ▶▶

"When Napster went down, Morpheus, LimeWire and Audiogalaxy quickly filled its shoes."

► old former Unix engineer who heads a non-profit organisation called Xiph.org Foundation that is developing open-source solutions for multimedia. Mr Plant surveys the codec scramble from above the fray. Surviving mostly on donations, Xiph.org is developing an open-source video codec called Tarkin. What really defines the success of a codec, Mr Plant believes, is its ease of use, adaptability and popularity. He argues that the average consumer wants something that looks and sounds good, and does not care how the film is compressed.

Mr Plant compares Tarkin to Linux, the open-source operating system that has revitalised the Unix community and become a serious alternative to Windows. Linux got a foothold among computer-science students, who were looking for a cheap way to learn programming and downloaded the free operating system. Later, as companies recruited the stu-

dents as software engineers, Linux infiltrated the corporate world and took over many of the more important server duties there.

Xiph.org sees Tarkin following a similar path. The idea is that as more and more programmers download the codec for use in video playback devices, they will make continual improvements to its freely accessible software. Mr Plant contends that an open-source project such as Tarkin is more likely than a commercial project to produce a high-quality codec, because the motivation behind such volunteer groups is not profit but performance.

Whether Tarkin—or any other new codec technology—succeeds will depend not only on the ingenuity of mathematicians devising the new algorithms for compressing video data and the talents of the marketing people who are seeking to build the brand. Equally important will be getting the backing of those who con-

trol the means of delivery: the cable companies. Without a conduit into the home, content providers are stymied. Most cable operators have already made big investments to add digital cable and high-speed Internet services to their networks. Providing for video-on-demand means spending millions more.

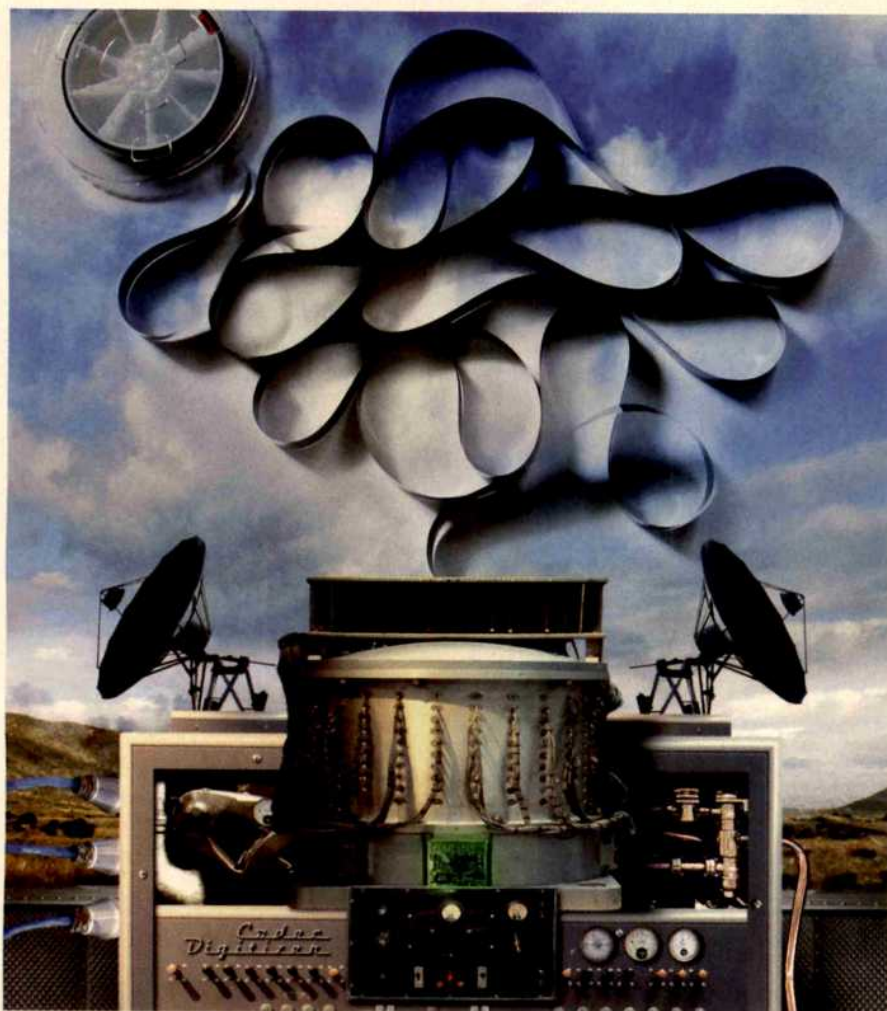
Fortunately, a short cut is in development at CableLabs, an industry R&D consortium that includes AOL Time Warner, AT&T Broadband, and Comcast. The project, known as OpenCable, will establish a cable transmission standard analogous to the Internet protocol that will allow set-top boxes from any manufacturer to work with any cable system and swap movies, games and multimedia content. The devices would incorporate an array of features, including Internet capabilities and browsing software, to make possible video-on-demand services.

Avoiding music's mistakes

But first, content creators must agree on a method to encode their content for Internet delivery. At present, nobody is sure what form that will take. Will there be one principal codec, such as VP5, MPEG-4 or Divx, handling content and powering the majority of set-top boxes? Or will there be an array of codecs scrunching video that is encoded in a variety of formats?

That is not important, according to Mr McIntyre. He cites KaZaA, a piece of software that allows enthusiasts to swap video content over the Internet in a Napster-like fashion but even more anonymously. Already, 62m users have downloaded the KaZaA software. At any given moment, some 800,000 people are said to be sharing media files this way. As high as they are, those numbers will be minuscule, declares Mr McIntyre, if Hollywood and others waste any more time quibbling over formats, or fretting over copyright infringements.

In May, KaZaA announced that it would have to shut its doors because it could not find the cash to defend itself against the barrage of lawsuits filed by the studios. Will big media ever learn? When Napster went down, Morpheus, LimeWire and Audiogalaxy quickly filled its shoes. Consumer demand for content is not going to wait for the studios to sort out their gripes. Even if KaZaA disappears, its success proves that very soon video codecs will do for movies what MP3 did for music. Then it will be too late to persuade consumers to pay for a service they can get for nothing. ■



Spitting image

Engineering insight, dogged determination and a dash of serendipity have made the lowly inkjet imaging device the king of computer printers

IN THE annals of computing, nothing has caused as much disappointment as putting ideas on paper. For decades, printing computer files was a thankless task for users who were seeking to reproduce precisely what they saw on the computer screen. Then along came the inkjet printer that sprayed tiny dots of ink on to the paper—and so started a revolution in the printing of high-quality images that was more important than anything since photogravure.

Thermal inkjets, first commercialised by Hewlett-Packard and Canon in the 1980s, began as slow, messy machines that were no match for the costlier laser printers that had just been introduced. But eventually, the scrappy little inkjet printers got better and better. Today, an inkjet printer costing less than \$50 will spit out crisp colour pictures, sharp text and brilliant graphics as good as any laser printer costing 30-40 times more. No wonder inkjets outsell laser models twelvefold. Inkjet cartridges alone now account for \$19 billion of annual sales, according to Lyra Research, a consultancy in Newtonville, Massachusetts.

For all its originality, the idea behind the inkjet is far from new. As long ago as 1867, William Thomson (later known as Lord Kelvin) was granted a patent for "Receiving or Recording Instruments for Electrical Telegraphers" which used electrostatic forces to control the release of ink drops on to paper. In 1951, Siemens

produced the first continuous inkjet printer. And throughout the 1960s, other manufacturers unveiled improvements on the same idea—all with little success. Inkjets proved expensive, messy and unreliable, with pumps, bladders and other moving parts that simply could not deliver an affordable machine capable of producing high-quality prints.

The modern inkjet solved these problems with a self-contained print head, complete with inkwell, spraying mechanism and nozzles that could be controlled accurately. Throughout the 1970s, research into the technology focused on piezoelectric methods. These use special crystals that vibrate when charged to squeeze out controlled amounts of ink. The most compelling innovation, however, came when engineers turned to heat instead of vibration.

The thermal inkjet printer was invented not once, but twice. The idea was conceived simultaneously, and unbeknown to one another, by two competing teams on either side of the Pacific. In Japan, Ichiro Endo, an engineer at Canon, noticed ink squirting from the neck of a syringe when a hot soldering iron touched it. Thousands of miles away at Hewlett-Packard's laboratories in Silicon Valley, a researcher called John Vaught dreamed up his version of the thermal inkjet by borrowing from the mechanism of the coffee percolator.

Hewlett-Packard's efforts began on Christmas eve, 1978. Together with David Donald and a group of other engineers, Mr Vaught began idly to discuss concepts for an ideal printer. The team had just delivered the engine for HP's first laser printer and was working on a gravure printer for the commercial-publishing world. Despite this, the team wanted more—especially colour, speed and, most important

of all, low cost.

That was a tough combination. At the time, printers fell into two categories: impact and non-impact. Typewriters aside, the most common impact printers were dot-matrix devices, which used an array of pins to strike an ink ribbon to form characters or other images. Non-impact printers, by contrast, offered more hope. By not touching the paper when making an image, they promised to be more accurate and efficient.

Although far from mature, no fewer than five non-impact technologies were vying for success. There were inkjets that sprayed microscopic dots of ink through hundreds of tiny nozzles on to paper; laser printers that used a laser beam and the xerography process to affix toner to paper; solid-ink printers that employed a similar technique to melt sticks of a coloured wax-like ink on to paper; dye-sublimation printers that relied on long rolls of film, heated to embed dyes into special paper; and thermal autochrome printers that applied heat to a special type of paper already impregnated with dyes to produce colour prints.

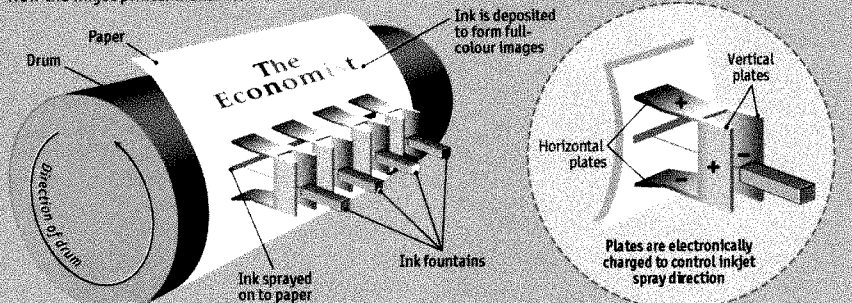
In 1978, the inkjet concept caught Mr Vaught's imagination, because it promised to yield a simple, low-cost and high-performance printer. Despite its shortcomings, the technology was considered to have far greater potential for improvement than its rivals. That afternoon, before departing for the Christmas holiday, Mr Vaught and his colleagues concluded that the ideal printer was an inkjet machine that could deliver 200 dots per inch and be capable of printing in full colour. Over the holiday, Mr Vaught set the ground rules: the new type of printer would have an array of ink nozzles spaced a two-hundredth of an inch apart and be able to feed ink fast enough to print one page per second.

Returning to the laboratory after Christmas, Mr Vaught focused on building a solid-state print head that would experience less wear and no clogging, but still be able to spit ink out fast enough for the job. As he watched a coffee percolator, he realised the answer was to use the ink itself to shoot dots on to paper.

To do so, he tried using a pair of electrodes with the ink between them acting as a resistor. The idea was to get the heat to vaporise a small portion of ink very near a nozzle, causing it to spit out a droplet. Unfortunately, the ink did not have high enough resistivity to create the necessary heat. Worse, the process electrol-

Little squirt

How the inkjet printer makes its mark



Sources: Canon; Hewlett-Packard

"The race to develop the inkjet printer had a profound cultural impact on both companies."

used some water in the ink into hydrogen and oxygen, which interfered with the operation.

Mr Vaught then tried harnessing the hydrogen and oxygen to produce a micro-explosion capable of firing the ink out of the nozzle. A small spark could be induced across the electrodes to ignite the hydrogen bubbles and spit out a drop of ink, but the process was nowhere near fast enough. In a third attempt, Hewlett-Packard engineers opted to put all the energy into the spark itself, in order to boil a bubble of ink. That succeeded, but the electrodes quickly deteriorated.

The breakthrough came when Mr Vaught and his colleagues seized on thin-film resistors. These were found to be able to produce enough heat to boil a bubble of ink and spit a dot out rapidly with a high degree of control. The resistors were mounted inside small tubes that were etched with grooves to create the nozzles, and switched on and off rapidly to spit out microscopic dots of ink. Within three months, the Hewlett-Packard team had concocted a workable version of a thermal inkjet mechanism.

Surprisingly, for all their engineering insight, the team could not explain exactly why their printer worked. And although it worked well, and was patentable without an underlying theory, Hewlett-Packard's middle managers were reluctant to invest in the idea. Some top HP managers dismissed the invention altogether. As it turned out, the physics of Mr Vaught's process—known as "phreatic reaction"—would not be understood fully for another year.

But Mr Vaught doggedly pursued his interest in the inkjet printer. He demonstrated his work to anybody who took an interest, eventually catching the eye of, among others, Larry La Barre, an HP old-timer who was able to persuade the company's management to take the technology more seriously. Thereafter, Hewlett-Packard started showering R&D funds on inkjet technology, and the programme became a critical part of its future.

Canon ball

Meanwhile, Mr Endo had already started work on a broadly similar effort. Canon's goal was to create better xerographic technology, inkjets being just one of several options. Back in 1977, Mr Endo and his team focused on fabricating a piezoelectric system that could send electronic pulses through a nozzle, creating enough

force to shoot ink from the chamber. But when a researcher accidentally touched the tip of an ink-filled syringe with a soldering iron, the squirt of ink changed the course of Canon's research and subsequent fortunes.

Within days, Mr Endo and his team used the discovery to build a simple inkjet printer that would come to be known as the Bubblejet. The main difference between this and HP's invention lay in how the ink was fired: Canon's shot ink out sideways, while HP's print heads released their ink from the top.

Two years later, Hewlett-Packard found out about Canon's work. The patents for many of the key inventions in both research efforts had been filed within months of one another. The result was a relationship between Canon and HP that continues to this day. Hewlett-Packard has borrowed some of Canon's designs for extending the life of the print head, while Canon has borrowed from HP's ideas for print-head configuration. Despite brief disagreements over rights to the technology, Hewlett-Packard insists that the co-operation has developed into a healthy competitive relationship between the two companies, and moved the state of the art further than it would otherwise have gone.

Following the two initial inventions, the development of inkjet technology became a multidisciplinary effort. New quick-drying and light-fast inks had to be developed. Improvements in the print jets continued apace. Better mechanisms for feeding the paper, and new software to improve image quality, were added. To raise speed still further, engineers on both sides developed faster motors and lightened their print-head mechanisms, while increasing the number of nozzles on their heads. More features were added to the inkjets, and soon hybrids of the technology that turned printers into fax machines and copiers emerged. Today, multifunction machines are the fastest-growing bit of the printer market.

The race to develop the inkjet printer had a profound cultural impact on both companies. For instance, disposable print heads, developed in 1984, are said to have caused no end of grief at Hewlett-Packard. The very thought of disposing of the little plastic units that contained the printers' intellectual property was anathema to some of HP's executives.

Other competitors entered the market with designs of their own. Epson introduced its inkjet line based on piezo-

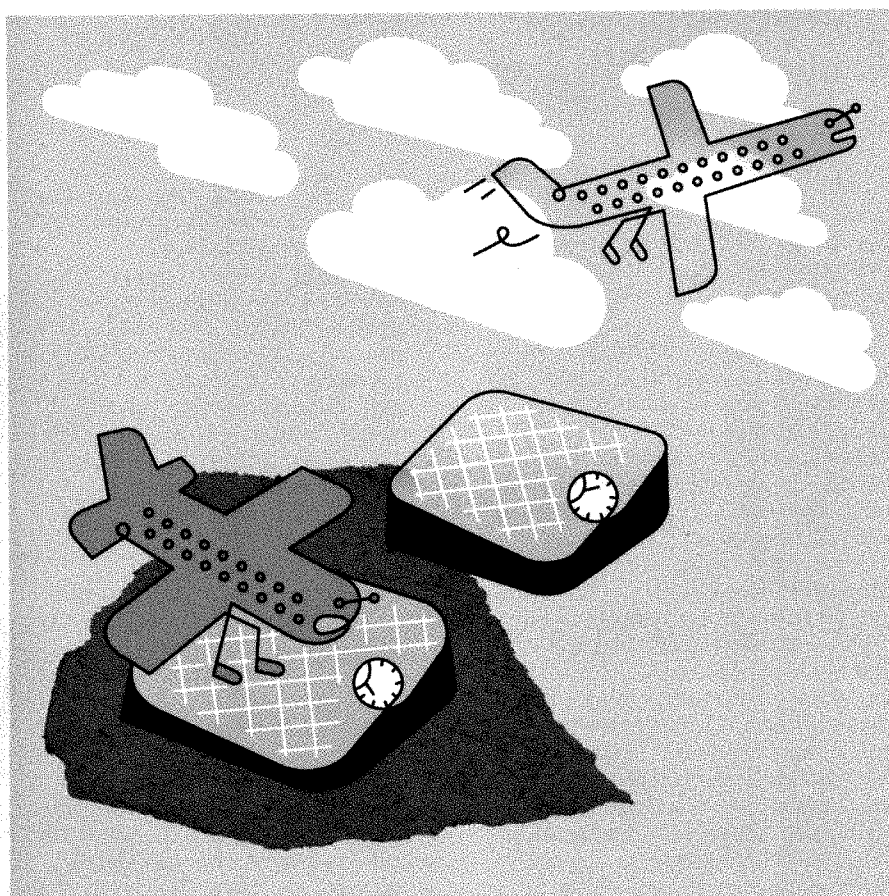
electric technology first investigated in the 1970s. Lexmark and Agfa also jumped in, focusing on specialised applications such as digital photography and graphic arts. But for all the interest, the growth of the inkjet market got off to a poor start. Compared with Hewlett-Packard's Laserjets, which were seeing healthy sales growth, the inkjet market appeared to languish after the company created its first Deskjet range in the late 1980s. At one point in the mid-1990s, HP even pondered pulling the plug.

Colour to the rescue

The widespread use of colour in computing during the mid-1990s changed everything. Just as Mr Vaught had planned, adding colour capability to inkjets was the next logical step. Print heads with complementary colours of magenta, cyan and yellow were added to black ink, enabling printers to create a full range of colours. More specialised photo printers have also added various shades of the primary colours to produce ever more faithful reproductions. "We essentially took all the work of craftsmen in a printshop and put it in algorithms," says John Meyer, a director at HP's laboratories. As computers became ever faster, those algorithms allowed prints to become sharper and ever more vibrant.

Today, the inkjet is no longer a cheap substitute for a laser printer, but a graphics machine in its own right. The average print head now contains more than 300 nozzles and is capable of producing images with a resolution of at least 1,200 by 1,200 dots per inch—more than the eye can resolve. The average machine can now fire ink at a blinding 14,000 dots per second, depositing more than 1m drops of ink on a square inch of paper. Most of the development work is now going into creating durable, light-fast inks to prevent pictures from fading. Meanwhile, new software is helping to produce clearer pictures by controlling the printing pixel by pixel.

Ultimately, the development of the inkjet printer underscores how lateral thinking can yield remarkably simple solutions to complex problems. Both Mr Endo and Mr Vaught, who have shared numerous industry awards in recognition of their accomplishments, displayed dogged determination and belief in their inventions, despite much internal resistance. But in doing so, they revolutionised the computer business and brought colour to people's lives. □



Desperately seeking lightness

Composites: As they struggle for market leadership, Boeing and Airbus are having to rethink how they make aircraft, and what materials they use. Airbus is taking the bigger gamble, with its new super-jumbo, the 550-seat A380

SINCE Boeing acquired McDonnell Douglas in the mid-1990s, there have been only two aircraft companies (Europe's Airbus Industrie being the other) that are capable of building commercial jets with more than 100 seats. Over the next 20 years, the market for such aircraft is expected to be at least \$1.2 trillion. Which of the two will take the bigger slice of that market?

There are few engineering tricks left that could give one or other a technological edge. There is little to choose in terms

of the aerodynamic efficiency of their designs. The engines they use are identical. The latest version of either company's aircraft is only a few percentage points better than its predecessor. Long gone are the days when Boeing's 747 jumbos almost quadrupled the productivity of the Boeing 707s and Douglas DC-8s that they replaced, or the earlier doubling of productivity that those airliners made over piston-engined planes.

On top of that, customer finance is more or less equal. Government agreements now prevent flagrant subsidies on both sides of the Atlantic. Of course, the American and European governments still underwrite much of the research and development that underpins their respective aircraft industries. Even so, none of this has moderated the price war between the two companies.

It used to be argued that, once there was a clear duopoly in civil-aircraft manufacturing, aircraft prices would rise. That theory has been thoroughly discredited. The best indicator of new-aircraft

prices—the average price per seat, adjusted for inflation—has been declining for several years, thanks to brutal competition between the two rivals. According to *Airline Monitor*, the cost per seat declined by 11% in real terms from 1995 to 2001, even though there was a booming demand for new aircraft. That leaves only aircraft weight (and its close cousin, manufacturing cost) as the key area in which the two makers can innovate.

Boeing's latest attempt to do so is its Sonic Cruiser, a radically new (and lightweight) aircraft which is intended to fly close to the speed of sound—ie, around 15% faster than today's conventional jets. But, lacking sufficient support from cash-strapped airlines, the concept remains a paper aircraft for the time being. Meanwhile, Airbus is pressing ahead with the use of composites in its new A380, the 550-seat behemoth that is now in full development and should come into service in 2005. Jens Hinrichsen, the director of structures at Airbus's large aircraft division, claims that, as the design now stands, around 40 tonnes (18%) of the A380's structural weight will consist of carbon fibre.

Two to tango

Airbus's efforts are being encouraged by the European Union. Under the EU's Fifth Framework programme, aeronautical research was allocated \$630m for a five-year period ending this year. This programme includes the so-called Tango projects for encouraging the use of composite materials in civil aircraft, with the aim of cutting 20% from both the weight and the manufacturing cost of new European airliners. If that order of saving were achieved, it would be equivalent to an 8% reduction in direct operating cost.

Tango is split into four main projects: an all-composite wing, plus the structure where it joins the fuselage; two rival fuselage programmes (composite versus metal); and a composite centre-section box that joins the two wings at the base of the fuselage. The projects are clearly designed to support Airbus's upcoming P322 programme, a 110- to 180-seat design intended to replace the Airbus A320 family. The P322 is to be launched later this decade. But already, work on one particular Tango element—the centre-section wing box—has been accelerated so it can be used on the A380. Altogether, \$38m of Fifth Framework money is being spent on composite applications, plus an equal amount from the 35 companies participat- ➤

"The real pay-off is when the design is rethought to take full advantage of the composite's properties—not just its strength-to-weight superiority."

ing in the research programme.

If that sounds like a backdoor subsidy, it is. And Europe's increase in taxpayer support for aeronautical research is happening just as American taxpayers' support for aeronautics and composites research by their own aerospace agency, NASA, is in decline. It is no secret that the EU intends to use these programmes to help Europe gain the lion's share of the large commercial-aircraft market.

Crash diet

Shedding weight is crucial. For one thing, the heavier the structure the larger the engines needed to push it (and the extra fuel that is needed) through the sky. In turn, that means that less payload—passengers and freight—can be carried. Reducing the A380's structural weight by eight tonnes (around 3% of its weight) would cut 2% from direct operating costs—and on such differences are sales made.

A lighter plane is also quieter. That is because less power is required, and there is a smaller mass carving its way through the air. This second point is important when it comes to landing noise, since a lighter plane needs fewer noise-creating flaps and other devices to help it to slow down when landing. Moreover, a lighter

plane is cheaper to make, since it requires less of the expensive materials that are used in aircraft manufacture.

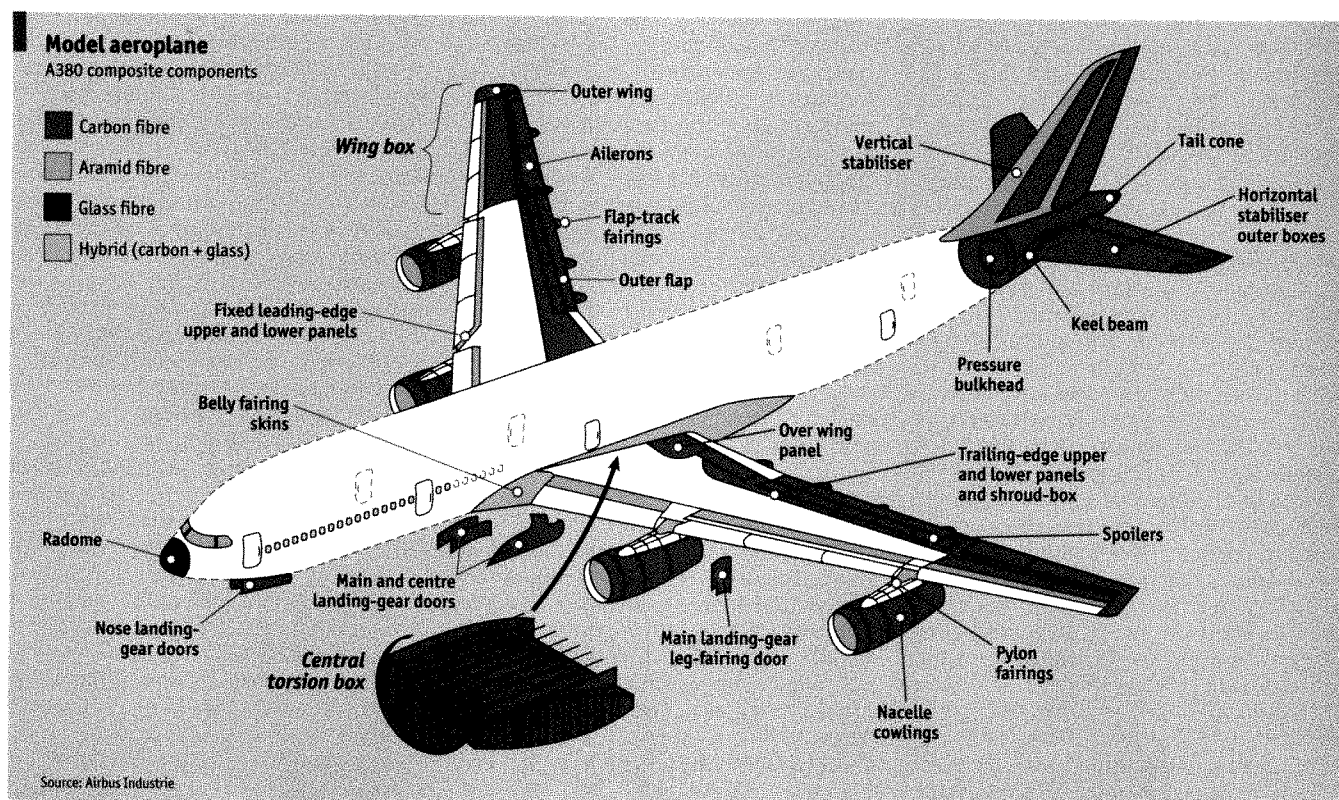
Composites offer designers a way to lose weight, thanks to their better mechanical properties. But costly composites cannot be justified throughout an aircraft. For instance, an earlier version of the A380 design planned to use composites for the outer wing section, while retaining a conventional aluminium structure for the inner section. This idea was dropped for two reasons. First, given today's composite technology, it was hard to beat the cost of an aluminium wing. Second, the heavy joint needed to ensure that the loads between the two parts of the wing were transferred properly meant that there was no significant saving in weight.

Apart from all the carbon fibre going into the A380, another 4% of the aircraft will be made of a new hybrid composite material called Glare. This is a sort of multi-layered sandwich made of sheets of aluminium foil interleaved with carbon fibre. When it designed the 777 in the early 1990s, Boeing rejected Glare because it was untried at the time. But since then, Glare has proved itself amply. At Airbus, the use of Glare in the A380 fuse-

lage will save 7% of the weight of the metal parts it replaces. It will also mean a much better fatigue performance (resistance to cracking caused by repeated flexing). The chart below shows where composite materials are to be used in the A380. What is clear is that composites have overcome doubts about the size of parts they are good for.

The rear of the plane is a good example. The A380's pressure dome—a 16-metre high bulkhead at the back of the double-decked cabin—is to be made by automatically laying fibres into moulds, a process well suited to structures involving double curvatures. The composite material for the job costs \$115-125 a kilogram, compared with \$20-30 a kilogram for the aluminium it replaces. But aluminium would require many panels, and the stretch-forming process used to make these involves a huge waste of material. The reduction in the number of panels also cuts assembly costs—in labour as well as in expensive fasteners. Better still, there is a 10% saving in weight.

The unpressurised section of the rear fuselage, between this bulkhead and the tail, may also be partly composite. Massive metal forgings and frames will be needed to carry the aerodynamic loads of ▶▶



"The question now is whether Airbus's technological assertiveness will win it the lion's share of that \$1.2 trillion feast."

the tail surfaces, but the skin and the rest of the structure (56% of its weight) will be made of carbon fibre. Instead of the 16 aluminium panels that are needed in a conventional metal design, there will be four composite panels, making a net weight saving of 12%. Airbus engineers expect a further 4% saving in the cost of assembling this section of the aircraft.

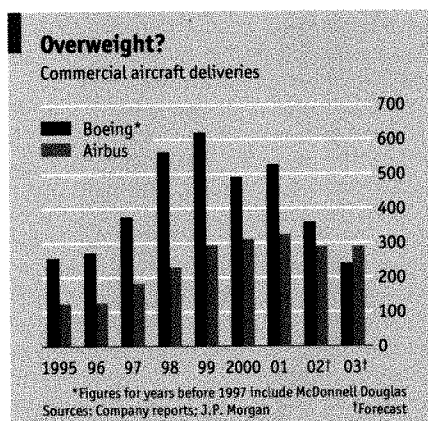
One of the biggest lessons that Airbus engineers have learnt is that the greatest savings accrue when the design of a part is not simply replicated in "black metal" (a reference to the shiny black colour of carbon fibre). The real pay-off is when the design is rethought to take full advantage of the composite's properties—and not just its strength-to-weight superiority. For instance, by careful design, components built out of a composite material can be made in a single, accurate piece, eliminating costly rework as well as heavy bolts and rivets. That means external surfaces can be a good deal smoother, reducing aerodynamic drag, and saving both fuel and further weight.

Several different manufacturing methods are being used for the composites on the A380. There are still a large number of parts in which the composite—mostly in the form of sheets and tapes of carbon fibres pre-impregnated ("pre-preg") with resin—is laid into moulds by hand. The size of the parts made by hand is limited, because of the difficulty in aligning the fibres accurately over large sections. As a result, hand-layup tends to be used for making one-off prototypes or for less critical parts of an aircraft, such as "fairings" that simply smooth the airflow.

Fewer hands, more machines

To save labour and produce composite parts with greater consistency, aircraft manufacturers are learning to automate their production processes. For instance, the floor beams for the A380's upper deck are to be made in Japan using a continuous process akin to extrusion. In "automated tape laying", pre-preg tape is wound into a mould or on to a mandrel. That works well for simple shapes such as circular tubes or box-sections. But for more complex shapes, a process known as "automated fibre placement" has to be used to wind the pre-impregnated fibre precisely around the component's intricate contours.

The result is very accurate, high quality parts—but at a price. Some of these parts require double-sided moulds. And all of them have to be placed in a vacuum



bag—to squeeze the air out of the resin and ensure good bonding—and then cured at temperatures of up to 200°C in a costly oven called an autoclave. To complicate matters even further, pre-preg composites have to be kept refrigerated up to the moment that they are wound on to a mould, in order to prevent the resin from beginning to cure.

Hence the trend towards so-called "resin infusion". This uses a single-sided mould into which dry fibre is placed. This material is then stitched together using techniques borrowed from the textile industry. Parts made in this way can be extremely complex. The "ribs" and "stringers" that form the inner structure of a wing can be sewn into place, with the fibres aligned precisely to gain the maximum strength. When the resin that bonds the fibres into a composite is injected, a complete part is made in one shot. This technique was demonstrated (on a Boeing 737-size wing) by NASA engineers as part of a \$300m programme that ran for ten years until 2000.

One novel technique that has caused a stir among aircraft engineers is a process developed by Quickstep Technologies of Perth, Australia. This uses a bath of heated water or oil instead of an autoclave to do the curing. The component being fabricated is enclosed in a vacuum bag and the internal pressure is then reduced moderately. The bag is dunked in the bath of heated liquid, which is then vibrated to ensure that all the air is shaken out of the resin so that a good bond can be made. Quickstep claims that this produces high-quality parts at a much lower cost.

A different approach to cutting costs is being taken by GKN, a British engineering company. One of GKN's American subsidiaries is applying basic production-engineering know-how to making

composite parts. It groups machines into "manufacturing cells" to get better throughput, and uses automated multi-axis machines to lay fibre, trim parts after moulding, drill holes and so on.

A generation behind

Composite technology today is where aircraft alloys were in the 1960s. Progress with the material is making rapid strides, but supplies are still limited. And the suppliers themselves are small, undercapitalised and due for a shake-out. No fewer than 800 suppliers from around the world had stands at a recent exhibition in Paris. The American Department of Energy reckons that the world market for aviation-quality carbon fibre is around 6,800 tonnes a year, with 60% of that going for military use. A quarter of America's F-22 fighter is made of fibre and over a third of the new Joint Strike Fighter will be made of composite. Even at a low production rate of two aircraft a month, the A380 will require a further 960 tonnes a year. Some industry insiders worry that this sudden increase in demand could outstrip supply. What will happen, they ask, if one of the large car makers comes out with a popular sports car made of high-grade carbon fibre—along the lines of the Lotus Elise?

Composites face other challenges as well. The metals producers are not standing still. Laser-welding and other fabrication processes are now being used to reduce weight and assembly cost. That alone probably makes an all-composite commercial airliner unlikely. Another problem for composites is how to repair them. Airlines need to have handy repair methods—akin to riveting patches over damaged parts—so that they can get damaged aircraft back in service quickly. There are also questions over how to detect potential weaknesses in composites, following the failure of the composite fin on an American Airlines A300 that crashed in New York in 2001.

For the time being, Airbus is ahead in using composites in commercial airliners. It has a record of being more aggressive than Boeing in adopting new technology. But, then, so did McDonnell Douglas—although its demise had more to do with low overall investment than taking technological gambles. The question now is whether Airbus's technological assertiveness will win it the lion's share of that \$1.2 trillion feast. One thing is clear, however: ensuring that it does is now official policy in Brussels. ■



Computers that run themselves

Computing: For decades, scientists have concentrated on making computers more powerful. Now they want to build systems that are smart enough to look after themselves

YOU want to dash for a bus on the other side of the street. But imagine that, instead of your brain automatically giving you a dose of adrenaline, speeding up your breathing and calculating all the right movements autonomously, you had to perform each of these functions as separate acts of conscious deliberation. The chances are you would stumble before even stepping off the kerb. In many ways, such is the state of information technology today—at least in IBM's view.

Computer systems and their "organs"—eg, microprocessors, applications and networks—are becoming ever more powerful. But they are also becoming ever more complex, and so have to be managed by a fast-growing army of information technology (IT) worker bees. This development has been a boon for IT services firms, and in particular IBM's Global Services, which now accounts for almost half of Big Blue's revenues. But these companies also know that simply throwing people at the problem is no solution. That is why, last October, IBM

launched an initiative called "autonomic computing", which is now starting to gain serious attention.

The goal is nothing short of building computer systems modelled on the part of the nervous system that is "autonomic"—ie, the part that governs involuntary body functions such as respiration and heart rate. "It's time to design and build computing systems capable of running themselves," writes Paul Horn, IBM's senior vice-president of research, in the initiative's "manifesto".

Welcome to the club, say competitors, especially Sun Microsystems (IBM's arch-rival), which claims to have moved along similar lines for some time. But Dr Horn's manifesto could, one day, be seen as marking the turning-point when the business started—after several unsuccessful attempts—to change its ways in earnest. Instead of focusing primarily on performance and new features, the industry now has a chance to spend more on making things actually work.

Recent marketing campaigns show that IT firms have suddenly discovered increased demand for things such as reliability and availability. Oracle praises its databases in adverts as "unbreakable". Microsoft wants to be the champion of "trustworthy computing". IT consultancies are pushing similar themes. Forrester Research of Cambridge, Massachusetts, recently coined the term "organic IT". By this, it means IT infrastructure "built on

cheap, redundant components that automatically shares and manages enterprise computing resources."

It is no accident that the IT industry should now be focusing on things other than raw performance. Chips have become so powerful, disk space so cheap and networks so fast that other aspects of computing have risen in relative importance. At the same time, the cost of downtime is increasing. A stockbroking firm can lose \$6m or more if its computer system is down for an hour.

Efforts to come to grips with the increasing complexity of computer systems are nothing new. In 1968, NATO sponsored a conference dealing with the "software crisis" which was said to be undermining the economy and defence of the western world. Then there was "fault-tolerant" computing, focusing on redundant hardware, which Tandem Computers (now part of Hewlett-Packard) turned into a business. Autonomic computing is meant to go further, embracing not just software and hardware but all parts of computing systems as well.

Feeling blue

In IBM's view, an autonomic computer system—itsself a collection of more or less self-regulating systems—needs to possess many of the characteristics of the human body. For instance, it must have an identity; be able to adapt to a changing environment; be capable of healing itself; and have an immune system. In computer terms, this means that an autonomic system has to know its own resources, and be able to reconfigure itself, to call up redundant elements in case of a malfunction and to destroy computer viruses automatically.

This is a tall order that will take decades to fill, as Dr Horn is the first to admit. But IBM's Thomas J. Watson Research Centre in Yorktown Heights, New York, is already working on the elements of such autonomic systems. One project is the firm's next generation of supercomputers, code-named Blue Gene. These machines will have more than a million processors, each capable of a billion operations per second (one gigaflop). Together, they will be 100 times more powerful than IBM's fastest computer today. As such, they will be capable of tackling some of the most complex problems imaginable—such as figuring out how proteins fold themselves into their distinctive shapes.

Given such a large number of proces- ➤

"The complexity of today's computing will, in the not too distant future, outgrow the human ability to manage it."

sors, on average one will fail every four days (usually as a result of damage by cosmic rays). But instead of requiring technicians to rush to replace them so that the machine can keep running during long computations, Blue Gene will be engineered to be fault-tolerant. In other words, it will detect failures and automatically reroute tasks to working processors.

Blue Gene will not be up and running before 2004 at the earliest. But the result of another IBM project called "e-workload manager" will probably make its way into customers' hands by mid-2003. The idea here is to allow a computer system to prioritise its responses to different requests—and, if need be, to reconfigure itself to fulfill them. An online stockbroking firm, for instance, could instruct its system to make sure that a regular customer always gets a quick response, especially when there are many one-time users online merely checking free stock quotes. Today, such things usually have to be configured by hand.

Similar technology is already part of IBM's mainframes. Now the firm's researchers are extending it to distributed computing. At the heart of such prioritising technology are "adaptive" algorithms that learn from data that the system has already generated—for example, the computing load required by certain requests. A big challenge, says Donna Dillenberger, one of the project's researchers, is to teach the algorithms what to forget—in short, to determine which data are noise and which form a trend.

Such a skill will be essential when attempting to meet the goal of another IBM research project called Océano: to develop the prototype of a "computing utility power plant". In contrast to today's shared-data centres, one main characteristic of these huge systems of thousands of server computers and data stores is to assign capacity dynamically—say, to an online shopping website during the holiday season.

Other computer firms are pursuing similar research—and, in some areas, are ahead of IBM. Hewlett-Packard, for instance, has a project called "planetary computing". Researchers at HP's laboratories in Palo Alto, California, are working on a data centre with as many as 50,000 servers. The plan is to have such computing installations spread across the world and linked via super-fast fibre lines.

This network of giant data centres, Hewlett-Packard hopes, will turn computing into a utility on a global scale. The sys-

tem would fire up servers whenever and wherever a customer needed additional capacity. It would place data globally so that it could be accessed anytime, anywhere. Moreover, it would monitor itself, automatically rerouting data traffic from a broken server to a working one.

Sun Microsystems, for its part, is already past the prototype stage. In the imminent future, the firm will introduce its much awaited "N1" initiative. This is essentially an operating system for data centres that turns the whole network into a computer—Sun's goal since its beginnings. Like HP's efforts, the core concept of N1 is to "virtualise" computing systems—building and rebuilding them as needed from subsystems such as servers and storage units connected to the network.

Broody computers

Research projects related to autonomic computing at universities are less grand, but often have more interesting approaches. Instead of building huge data centres, John Kubiatiowicz and his team at the University of California, Berkeley, plan to federate thousands of personal computers on people's desktops into one huge data store called OceanStore. Because encoded fragments of a file can spread over hundreds of hard disks, the file can still be reconstructed even if computers containing parts of it fail.

OceanStore is part of Dr Kubiatiowicz's research into what he calls "introspective computing". As the name implies, it is about enabling computer systems so that they can continuously monitor their own inner workings, analysing those data and optimising themselves so that they become less crash-prone. This raises the interesting possibility that a machine might have to "sleep" and even "dream" regularly to become truly autonomic.



The idea of recovery-oriented computing (ROC), an effort led by David Patterson, another Berkeley computer-science professor, is equally unusual. It is based on the premise that accidents happen. Software will always have bugs; hardware will fail sooner or later; and humans will invariably make mistakes. Instead of simply trying to avoid failures, Dr Patterson argues, computers should be able to recover from them quickly.

To make its point, the Berkeley ROC group built an e-mail system with an "undo" feature like that in most word-processing programs. It records all its activities. Should a virus crash the system, the administrator can rewind it and fix the problem. To make such binary time travel possible, the system has to save an enormous amount of data. But with hard-disk space so cheap, this drawback will make little difference.

Making computing really work is not just a question of technology, argues Dr Patterson. If the IT industry has managed to increase performance 10,000-fold in the past 20 years, he says, it is because such things as chip speed and storage capacity are easy to measure. But finding the right metrics for, say, the recovery-friendliness of a system is much more difficult. To start the ball rolling, Dr Patterson recently developed a simple way to estimate the cost of downtime—by computing the time wasted by employees who cannot get their work done because of computer problems.

There is another economic reason why autonomic computing might not be adopted as quickly as advocates would like. In the past, at least, IT firms had an interest in making computing more complex than was strictly necessary—in particular, by the way they made their equipment proprietary. But autonomic computing, says Dr Horn, will work only if the IT industry fully embraces open standards. That is beginning to happen, but only grudgingly and only where absolutely necessary.

Yet something rather like autonomic computing will surely exist one day, if only because the complexity of computing will, in the not too distant future, outgrow humanity's ability to manage it. This raises the question of how autonomic do users want their computers to become? The case of HAL 9000, the computer in the movie "2001: A Space Odyssey" which could be stopped only by pulling the plug, suggests that there ought to be some limits. ■

The other Bill



Bill Joy, networker-in-chief

For a quarter of a century, Bill Joy—"the Edison of the Internet"—has envisaged a world in which countless devices are wired together. Now he is trying to turn that vision into a reality, but not without warning of the risks to society

"OPERATING systems", Bill Joy once declared, "are like underwear—nobody really wants to look at them." For more than 25 years, the mantra that computing should remain simple and that operating systems should be hidden in the background has been a guiding principle for Mr Joy, chief scientist and co-founder of Sun Microsystems. That quest for simplicity has made him one of the most influential and prolific inventors in the computer business.

Part-scientist with the necessary scruffy hair and crumpled clothes, and part-businessman with a keen sense of marketing and strategy, Mr Joy has had a hand in developing almost every crucial technology for the Internet of the past two-and-a-half decades. He is also credited with dreaming up the technologies that made Sun what it is today. In the 1970s, he turned Berkeley Unix into the leading operating system for mainframe computers and servers. In the 1980s, he helped to design the Sparc microprocessor that is the heart of Sun's successful server business. In the 1990s, he spearheaded the development of the Java programming language for portable Internet applications. Today, he is leading the push into distributed computing, popularised by "peer-to-peer" techniques.

Through it all, he has focused on moving the complexity of computing from the desktop to the network where, he has long argued, it can be managed more easily, and without the user noticing. In 1988, that vision was crystallised in Sun's enduring slogan: "The network is the computer." In the decade and a half since setting Sun's agenda, Mr Joy's vision has turned the company into an \$18 billion powerhouse, with products that are the very heartbeat of the Internet itself.

If Mr Joy were to have his way, however, the future of computing would rest on a mere 50,000 lines of computer code that make up his year-old initiative called JXTA (pronounced "Juxta"), which seeks

to build standards and infrastructure for peer-to-peer computing. First announced in 2001, JXTA is the culmination of a decades-long effort to build and popularise the infrastructure for distributed computing. At stake, say proponents, is the complete rewiring of the Internet—an undertaking that promises to unleash a whole new wave of software innovation that Sun hopes to ride successfully.

Bill Joy's impact on computing began back in the mid-1970s at the University of California, Berkeley, where researchers were pioneering a new kind of computing architecture. Their aim was to make it easier for computers to communicate with one another—and, in the process, to encourage the development of what were to be called personal computers. Bill Joy, then a young man from Michigan, had opted to do his masters degree at Berkeley because the campus had the worst facilities of any that accepted him—and therefore, he felt, offered the greatest challenge. "At Berkeley," says Eric Schmidt, an old friend who is now boss of Google, an Internet-search firm, "there were graduate students, and then there was Bill Joy."

It was Berkeley Unix that made him a legend in the computer industry. The Unix operating system was developed at AT&T's Bell Laboratories in the early 1970s and had been distributed freely to government organisations and universities for use in their mainframes. At Berkeley, Mr Joy and his colleagues began tinkering with it to fix bugs in the code. Their improvements quickly caught the eye not only of other universities, but also of the Pentagon. In 1978, Mr Joy and his colleagues were awarded a contract by the Defence Advanced Research Projects Agency, to develop an operating system that could connect Digital Equipment's widely-used VAX superminicomputers into a fledgling network that DARPA called "the Internet".

By integrating a recently-devised communications protocol called TCP/IP with his version of Unix, Mr Joy helped to lay the foundation for the popular use of the Internet. In short order, the Berkeley Systems Distribution (BSD) of Unix became the most widely used operating system of its day. Even now, the various incarnations of BSD remain the main rival for Microsoft's NT/2000 operating system on servers. It is also the basis of Apple's OS X operating system.

Fast forward to 1982, when three Stanford graduates, Vinod Khosla, Scott

"As technology becomes ever more accessible to ever more people, they become ever more reliant upon it."

▶ McNealy and Andreas Bechtolsheim, persuaded Mr Joy to create the software for a cheap but powerful computer they had built called the S.U.N (short for Stanford University Network) workstation. The Stanford trio hoped to take Unix from the realm of universities and research laboratories into industry. And while the group never expected Mr Joy to be a wizard chip designer as well as a software genius, two years later he and a colleague, David Patterson, developed a new microprocessor that raised number-crunching to a new level of performance. Ever since, Mr Joy's RISC (reduced instruction-set computing) processor has been the mainstay of the company's \$10 billion server business. In the process, Sun Microsystems has become the world's leading supplier of networked workstations.

From the beginning, the central theme in Mr Joy's work has been to tie microprocessor-controlled systems together into a unitary whole. As early as 1978, he envisaged a world in which electronic devices would be sprinkled into everything, from thermostats and washing-machines to shoes and clothing, all communicating with one another in a sort of information ecosystem. To make this happen, he seized on the concept of "distributed computing" (ie, peer-to-peer computing) to unleash the power of every device, while allowing computational problems to be broken down into smaller, more manageable pieces.

At the time, such an idea seemed ridiculous. Desktop computers were simply not kitted out for such work. Besides, the notion of tethering independent computing devices into a single system was fraught with management problems. For instance, there was no way of telling which unit was working and which was not, or which processor was actually managing the resulting network and how it might pass control to another processor if it went on the blink.

The first clue as to how to make distributed computing work came in the 1980s, when Sun started developing a new operating system, called Oak, for interactive television—an application that proved to be ahead of its time. But by the early 1990s, when the World Wide Web took off, Mr Joy realised that Oak held the key. Building on that, Sun came up with a new programming language called Java. This permitted information to be shared as "objects", complete with data and a way of analysing them.

Java's attraction was its ability to

create small, efficient programs that could be sent easily over the Internet and, in theory, run on virtually any machine. Its simplicity, Mr Joy insists, helps to produce far more reliable and more secure programs. That makes them ideal for small, embedded computing systems such as mobile phones and portable gadgets. In 1999, Mr Joy took his vision a step further with Jini, a networking technology that uses Java to make connecting devices together much easier—allowing, say, a digital camera to communicate directly with a printer without having to use a PC as an interlocutor.

Juxtaposed

In the three years since Jini was introduced, the concept of peer-to-peer computing has itself gained ground, thanks largely to the growing power of personal computers. Today, even the simplest of computing devices has more than enough processing power to connect direct to other processors, without needing the help of a central server.

But once peer-to-peer computing became a fad, dozens of companies, each with its own proprietary system, rushed for a piece of the pie. The chaos threatened to make the whole thing unworkable. What was needed, argued Mr Joy, was an organisation to build the foundations for this new style of computing, allowing the peer-to-peer companies to do what they do best—develop applications.

Hence JXTA. With his colleague Mike Clary, Mr Joy secretly launched the project in 2000 as a way of organising software developers and establishing standards for peer-to-peer computing. All told, JXTA is based on six protocols that let peers (ie, individual computers) find one another and organise themselves into groups. Ultimately, it appears rather like an operating system for running a peer-to-peer network. Mr Joy likens it to the TCP/IP stack of software that he added to Unix in 1982 so that computers could connect to the Internet. And, as happened with BSD Unix, Mr Joy is determined to make his open-source JXTA the standard for peer-to-peer networking.

What does Sun get out of this charitable undertaking? Mr Joy insists that Sun does not intend to make money out of JXTA. What it would like to do instead is create a market that would generate a demand for its products and services. Yet, if peer-to-peer is intended to bypass servers, surely JXTA can only nibble away at Sun's core business of selling such ma-

chines? Mr Joy believes not. He insists that it will boost demand for servers in high-value applications such as transaction processing and databases, where centralisation is indispensable.

The corollary to Mr Joy's quest for simplicity is that, as technology becomes ever more accessible to ever more people, those people become ever more reliant on it. This has begun to trouble him. He fears that the speed of technological development may exceed humanity's moral and mental capacity to control it. He first fretted about this in an article for *Wired* entitled "Why the future doesn't need us". In particular, he wrote of the dangers of the "GNR (genetic nanotechnology robotics) revolution", saying that this putative technology could smother the human race into extinction. "This is a story that discovered me," Mr Joy admits. "I just happened to discover that what I saw as a problem no-one else seemed to be talking about."

Mr Joy was just blocks away from the World Trade Centre on September 11th 2001. For him, the events of that day were a clear warning of the risks people face in the modern world. Being singular in nature, such events are almost impossible to prevent scientifically. And yet, technology proved to be the enabling force for those who wished to harm others. "Bill's job is to challenge the conventional wisdom," says Mr Schmidt. "He has been thinking about these things for years, but it took until now for all of them to come together." Bill Joy's message is simple and succinct: "We must keep our euphoria with technology in check." ■



Sceptical enthusiast



The countryside

Charge of the green welly brigade

Crisis in the countryside? Hardly

RAP music and homosexuality are not the best-known pastimes of Britain's countryside campaigners. But in the run-up to the "Liberty and Livelihood" countryside march in London planned for September 22nd, anything to dispel the stereotype that the movement consists of brutal toffs is welcome. At a rally outside Parliament on Tuesday, hunting horns tooted and well-bred voices raised cheers to welcome an impromptu recital by Samuel Payne (nicknamed "the President"), a black American singer who has become a prominent supporter of the protest. "Our secret weapon—soooo hard for Labour to explain away," said one campaign official.

As a green jeep circled Parliament Square, towing an ingeniously constructed electric bonfire, an excitable elderly woman in galoshes spoke enthusiastically of her gay and lesbian allies. Their group, Hunting Pink, is a pun on the name for the foxhunters' traditional scarlet coats, which could become little more than fancy dress if the government bans the sport, as it proposes to. "The gays like hunting because they can dress up—the same reason that they become priests," she explained, in an ambitious lunge towards tolerance.

The proposed ban on hunting is only one of a number of grievances the marchers are bringing to town. There is, they say, a "crisis in the countryside". The rural economy is suffering from a depression in agriculture, plus the aftermath of the government's disastrous handling of the foot-

and-mouth outbreak last year which cost other businesses billions of pounds, and the pedantic enforcement of burdensome new regulations. Farm incomes have halved since the mid-1990s. Weekenders and outsiders moving to the country drive up house prices so that locals can no longer afford to live where they grew up. Villages become dead middle-class ghettos for commuters and oldies, and the government does nothing to stop this happening.

But the countryside doesn't get quite as rough a deal as the campaigners make out. For a start, farmers still receive £3 billion (\$4.6 billion) in direct subsidy, plus another £250m to help them diversify and restructure. There are programmes for the rural economy as a whole, too. One such aims to find the 25% of rural areas with the worst productivity and raise them to the national average, through a mixture of grants, loans and training. Given the difficulties involved in defining productivity, let alone raising it, that seems a tall order. Luckily this is costing the taxpayers a mere £40m a year.

Although the state spends about 20% more per head on public services for town-dwellers, that is largely because people in towns are poorer and sicker than those in the countryside, and more of them are foreign (which puts up the cost of educating them). Public services tend to be better outside big cities. Patients wait longer to see a doctor in London and the (largely urban) West Midlands than they do any-

where else in the country. Waiting times are shortest in Wales. According to league tables on the performance of police forces in England and Wales published this week by Policy Exchange, a think-tank, the West Midlands and London came 37th and 40th out of 42: Dyfed and Gwent (Wales again) were first and second. Urban schools tend to be worse, too. That's why so many parents of young children move out of the cities. Not many move in the other direction.

Basic public services aside, there are plenty of subsidies, hidden and overt, that prop up life in the countryside. The state spends nearly £100m a year on rural bus services—many of which carry very few passengers. The rural post-office network loses £25m a year. Another £30m goes to beefing up rural policing.

Reports of the death of the rural economy have been somewhat exaggerated. Farmers have certainly had a bad time in recent years. Over the six-year comparison favoured by the farm lobby, the decline in incomes does look dramatic. But this is hardly fair. Sterling was exceptionally weak in 1996-97, and prices for farm goods very high. Now the pound is strong and prices low—but in a cyclical industry, that is only to be expected.

Furthermore, although farmers' incomes have been dropping, the value of their assets has risen by around 40% since 1992. Sean Rickard, a former chief economist at the National Farmers' Union, now at the Cranfield School of Management, notes: "the average farmer sits on net worth of £700,000. Most of them could afford to retire more comfortably than most people in this country. What they are really asking is that we subsidise a way of life that they can pass on to their sons."

Outside farming, much of the countryside is thriving, especially in businesses that have managed to stay clear of the government. Henry Lang, a Somerset farmer, ►►

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realised in the mid-1990s that he would make more money farming buildings. His converted barns are now home to seven small outfits, in fields ranging from soft-ware to tapestry, with nearly 40 workers compared with just one on his 1,300 acres. Michael Brown, owner of the largest business, a smokery, says the countryside is a "brilliant" place to do business.

Population flows are a good indicator of where people think life is better. Each year, 100,000 Britons move to the countryside. Without the recent influx of foreigners, London would still be shrinking, as it was for decades, and as most other British cities still are.

Scotland's hunts

Riding for a fall

EDINBURGH

Foxhunting is already banned in Scotland. Not that you'd know it

ENGLAND'S foxhunters predict numberless disasters in the countryside if hunting with hounds is prohibited. Hunts will be disbanded. Thousands of fox-hounds will be slaughtered. Hundreds of hunt workers will be out of a job. So why has none of this happened in Scotland, which banned traditional foxhunting in March this year?

Scotland's prohibitionists wanted to ban all hunting with dogs. But the green-welly brigade persuaded them that, if foxes were to be controlled, dogs still had to flush them out, and a gun could finish them off. As a result, hunting is illegal only if done purely with dogs and horses. Use a gun, and you can claim the loophole left for pest-control. The Duke of Buccleuch Hunt, the oldest of the ten traditional Scottish fox hunts, has been out several times since the ban and expects to kill 60-80 foxes this year, much the same as before the ban was implemented. The local police force seems quite content that the new law is being observed.

Hunt followers on horseback seem to enjoy the new routine pretty much as they did before. There is every prospect that English and Welsh hunt followers will be able to do the same under the law planned by the government in Westminster. Alun Michael, a junior rural affairs minister, says the government wants to strike a balance between "recognising utility" (the need to control foxes as a pest), and ending unnecessary cruelty.

The huntsmen maintain their stiff-upper-lip determination to carry on partly because they still hope that the ban on hunting can be overturned in the courts. Although the first legal challenge was

Oddly, the popularity of rural life is one of the protesters' main gripes: that outsiders drive up the cost of housing for locals. Richard Burge, who heads the Countryside Alliance, the lobby group organising this weekend's march, believes that "if you can earn a living in the countryside, you have the right to buy a house that you can bloody well afford."

Short of restoring feudalism, or covering the countryside with cheap new homes (which the protesters, naturally, oppose) that seems fanciful. It is sad but true that, the poorer you are, the fewer choices you have about where to live—in cities or in the countryside. ■

thrown out by a judge, the hunters plan to pursue their case relentlessly, all the way to the European Court of Human Rights if necessary. English courts can expect similar sport.

It is not clear that the fox has benefited from the subtle change of practice in Scotland. Being chased, exhausted and ripped to pieces by a pack of fox-hounds clearly "compromises the fox's welfare" (to use an official commission's wonderful phrase). But being chased, exhausted and shot does not sound a whole lot better. ■



Over a hill and through a loophole

Smuggling

Anything to declare?

Customs officers' powers are excessive, but so is smuggling

RICHARD EVANS, a retired lorry driver, and his family were travelling in Spain last summer when their camper van broke down. They left it to be brought back by the AA. But customs officers at Dover claimed it was being used for smuggling. They seized the vehicle and all its contents, including 9,000 cigarettes and 20 bottles of spirits. The van, worth £20,000 (\$30,800), is still impounded. It even took Mr Evans six months to recover his 90-year-old mother-in-law's wheelchair.

Under European Union regulations, people may import an unlimited quantity of alcohol and tobacco, so long as it is for their own personal use. Had Mr Evans been driving his van himself, he would probably have had no trouble.

Cases like this are putting Customs and Excise's considerable powers under scrutiny. A recent stinging High Court judgment about another vehicle seizure said, "the mindset of those determining these policies has not embraced the world of an internal market where excise goods can move freely across internal frontiers." And, on September 18th, the EU announced that it was giving Britain two months to prove that customs officers were not breaching consumers' rights to shop freely in Europe. "Cross-border shopping...is a fundamental right under EU law and should not be regarded as a form of tax evasion," said Frits Bolkestein, the internal market commissioner.

Customs officers have an impossible job. Excise duty and VAT on a pack of premium brand cigarettes account for 79% of the recommended retail selling price of £4.51. An identical pack costs £1.97 in Belgium. One in every five cigarettes smoked in Britain—some 17 billion altogether—has been smuggled. The Tobacco Manufacturers' Association reckons that 80% of hand-rolling tobacco is smuggled.

The main weapon Customs and Excise has in tackling abuse is to seize cars in which it suspects goods are being smuggled. Guidelines suggest "personal use" can mean only up to 800 cigarettes, for example. Anyone bringing in more can be asked to explain. In the past three years, customs officers have impounded more than 22,000 vehicles. Tellingly, only a fifth of seizures are contested, and fewer than 1% of appeals are successful. Officials say the value of cross-channel smuggling has fallen sharply in the past year, from £1.6 billion to £400m.

Some customs officers, though, have clearly been over-zealous. And the recent High Court case ruled that the legislation under which Customs and Excise operates wrongly reverses the burden of proof. The defendant must prove that he is not bringing in tobacco and so forth for a commercial purpose. It also said that customs officers must have "reasonable grounds" for searches: suspicion and instinct are not enough. The government is appealing.

The minister in charge of Customs and Excise, John Healey, accepts that there is an urgent need to respond to questions about the "legitimacy" of the Customs regime. But he says the charge that Customs are abusing their powers is wrong: "Customs," he says, "never stop at random, they never do blanket searches. They always have some ground for stopping people." Tell that to Mr Evans. ■

Gays

Come on out

They are bothering both Anglicans and Tories

HOMOSEXUALITY hardly seems the most pressing issue facing either the toothless Conservative Party or the declining Church of England. But both institutions—ancient, prominent and troubled—are now embroiled in an argument about their attitude to a subject that most outsiders find bewilderingly peripheral.

For the Tories, it is a question of what to do about Section 28, a strongly worded piece of legislation passed in 1988 by the last Conservative government, which forbids the promotion of homosexuality in schools. Prompted by the fear that trendy local authorities were using sex-education lessons to pervert children's minds, it is unpopular with teachers, who say it makes it hard to answer pupils' questions about homosexuality.

A government attempt to repeal the clause failed this summer in the House of Lords. Another try is planned, which modernising Tories want their party to support. This would fit nicely with the party leader Iain Duncan Smith's plan of portraying a new sympathetic image, replacing a narrow appeal to family values with explicit tolerance towards both homosexuals and heterosexual sex outside marriage.

Traditionalist Tories are horrified by the party's shift. David Davis, a leading front-bencher demoted by Mr Duncan Smith in a clumsy reshuffle this summer, wants the party to stick up for Section 28. That may be popular with many of the party's existing supporters, but make

More BBC

Quantity and quality

One BBC channel produces just what a public-service broadcaster should

THE government was busy approving the BBC's expansion plans again this week, this time to launch another digital television channel, BBC3. Along with BBC4, a highbrow channel, and two new children's channels, CBeebies and CBBC, the BBC now considers its matching suite of digital channels complete. But BBC3 and BBC4 in fact illustrate sharply differing pictures of the broadcaster's future.

A year ago, the government rejected the

proposed BBC3, designed for 25-34-year-olds, because it was "not distinctive enough" from the commercial sector, where young people are the demographic holy grail for advertisers and broadcasters. Channels Four and Five favour them and plenty of pay-TV channels cater for them: Sky One, E4, Kerrang, Kiss TV, Paramount Comedy, Smash Hits, Bravo, Trouble, MTV, MTV Base, MTV Dance, the list goes on. BBC3, such channels claimed, would steal their audiences, and so depress their ad revenues.

A revamped bid has changed the government's mind, though. It accepted advice from the Independent Television Commission that the loss in advertising to the commercial sector, at £7m (\$10.8m)—or just 0.2% of all TV advertising revenues—will be "manageable". It also imposed 12 conditions on BBC3: 80% of output must be specially commissioned, for example, and 90% made in Europe. The minister for broadcasting, Tessa Jowell, says BBC3 must concentrate on bringing new material to the screen "not on competing for well-established programmes" (in other words the American imports aired by the commercial channels). So cult American series such as "24", which, after a first weekly airing on BBC2, was repeated each week this year on BBC3's prototype, BBC Choice, would be frowned on in future.

Contrast the BBC's ambitions for BBC3, however, with its performance at BBC4, launched in February this year. This channel, whose tagline is "a place to think", was always designed as something "that the commercial market would never do", says Roly Keating, its controller and formerly head of arts at the BBC. Its first week's schedule indeed verged on a parody of non-commercial TV, with township opera from South Africa and a performance by a Senegalese singer in an Islington church hall. A top-rated show will typically draw some 50,000 viewers—almost negligible in television terms.

Yet that narrow appeal makes BBC4 a model of what a publicly financed broadcaster ought to do. It has roamed into territory where its ratings-driven sister channel, BBC1, seldom dares to tread. Despite a tiny £35m budget, it boasts an intelligent prime-time talk show and a world news programme so internationally minded that its London provenance is barely visible. The channel attracts such varied participants as Tom Stoppard, Arundhati Roy, Jeffrey Sachs and Naomi Klein.

BBC4 may wear its gravity a little too heavily at times, but it supplies a variety and thoughtfulness unavailable on prime time BBC1. The more the BBC flagship channels chase the ratings, and the more that BBC4 refuses to be dictated to by them, the more the channel looks like a model for what a slimmed-down version of BBC television could look like. ■



Bishops tutu

it harder to gain new ones.

The shambles is mirrored in the Church of England, where the new archbishop of Canterbury, Rowan Williams, takes a soft line on homosexuality that also infuriates traditionalists. This week the outgoing archbishop, George Carey, warned of a split in the church if Mr Williams continues to support reforms that would, for example, allow the ordination of openly gay men to the priesthood, or the blessing in church of homosexual marriages.

In reality, there are already plenty of excellent homosexual priests who make little effort to disguise their domestic arrangements. The real difficulty for the church is that homosexuality, like all sex outside marriage, is explicitly condemned in the Bible. For many believers, abandoning that position for something more pragmatic seems a painful retreat into uncertainty.

Bagehot Saddam's feint

Iraq's volte-face has made life tougher for Tony Blair



THE suggestion made by Iain Duncan Smith, over tea last week with Tony Blair on the terrace overlooking the garden of 10 Downing Street, that they might join forces during Tuesday's Commons debate on Iraq to see off the appeasers and the fainthearts was met with a smile and the politest of "thanks, but no thanks". Mr Blair, as he demonstrated in an impressive speech to the trade union movement, has never been reluctant to confront his own party when he has deemed it necessary. And, besides, he was then confident that the tide of argument would be running strongly for him by the time that Parliament was recalled.

And so it seemed until the Iraqis' sudden, but largely predictable, volte-face over weapons inspection. President George Bush, prompted and encouraged by Mr Blair, had dramatically engaged with the United Nations; there seemed every prospect of a sufficiently tough new resolution from the Security Council to sanction, at least implicitly, the use of force against Iraq; and even Egypt and Saudi Arabia, stridently opposed to war only a week or so earlier, seemed intent on joining the fast-rolling anti-Saddam bandwagon. With opinion polls showing a pronounced shift in support for British military involvement in the toppling of Saddam Hussein, and with the imminent publication of the long-awaited "dossier" on Iraq's weapons of mass destruction, Mr Blair could regard the one-day debate, which he had only reluctantly conceded, with some equanimity.

It all looks different now. Having appeared to be in control of events, Mr Bush and Mr Blair are, at least temporarily, on the back foot. But the problems created by Iraq's declared willingness to accept the return of inspectors "without condition" are much greater for the prime minister than they are for his chum in the White House. Despite the almost universal belief that no proposal coming from Baghdad should be treated with anything other than the greatest possible scepticism, as Mr Blair prepares for both Tuesday's debate and, the following week, the Labour Party conference, he must realise that the terms of political trade have changed.

It's not that Mr Blair need fear anything so definitive as a vote in Parliament on his policy. Although dissident Labour MPs may find a way of registering their opposition through a procedural motion, unlike Mr Bush, the British prime minister is not con-

stitutionally required to gain the support of the legislature before committing his armed forces to action. Historically, declarations of war are taken under something called the Royal Prerogative. Theoretically, these are decisions taken by the sovereign (although, in fact, they are the prime minister's) which are therefore, amazingly, not subject to the scrutiny of Parliament. Constitutional reformer though he may be, Mr Blair seems quite comfortable with this notion.

The difficulty for Mr Blair is that the party he leads has a degree of faith in the UN that comes close to matching its sentimental passion for the National Health Service. Having made the case so strongly for building support for action against Iraq among "the international community" and placed such importance on getting the quasi-legal blessing of an appropriate Security Council resolution, Mr Blair has little choice other than to remain committed to that process. All will probably be well if a resolution of the kind that Britain and America are demanding (one that gives coercive powers to the inspectors, lays down a tight timetable and carries the unambiguous threat of armed intervention the moment the Iraqis start playing their old games) can be bullied past the foot-dragging Russians and French.

But whatever sort of resolution is passed, there is almost certainly a majority of Labour MPs and, possibly, cabinet ministers as well, who will expect the weapons inspectors to be given a reasonable amount of time to do their work before even contemplating what should come next. Most of the Labour Party thinks that there is now a real opportunity to avert war and will demand that it is not spurned—a view Mr Blair will find hard to ignore even if he shares Mr Bush's belief that the chances of the inspectors succeeding in their task are minimal.

So much easier for Bush

Even on the Tory side of the House, for all Mr Duncan Smith's uncomplicated support, a surprisingly large number of MPs have considerable misgivings about war with Iraq. In their case, it is not so much naive devotion to the UN that motivates them, but atavistic anti-Americanism (Suez is not forgotten), long-standing sympathy for conservative Arabs and distaste combined with envy for what they see as Mr Blair's grandstanding with the American president. There is also genuine dismay that their leader's complaisance has resulted in many legitimate questions—what sort of post-Saddam Iraq is envisaged, for instance—going unasked.

By contrast, Mr Bush has far greater room for domestic political manoeuvre. Although the chances are that he will conclude, however tetchily, that even in the absence of a satisfactory resolution, the inspectors should be seen to have failed before a military campaign begins, he is not bound by even that constraint if, as seems certain, Congress gives him a fairly free rein. If a divided Security Council becomes an obstacle to action, he will bypass it. At that moment, he will expect the British, if nobody else, to be with him. Mr Blair's worry is that, at that moment, most of his party won't be.

Even if things become as messy as this, Mr Blair is unlikely to deviate from the path that he has chosen. He will take his party on if he has to. Such is Mr Blair's dominance of British politics that he is likely to prevail. His job is probably safe as long as the Americans do not lead him into disaster. But, uncomfortably, the prime minister's destiny is increasingly in Mr Bush's hands rather than his own. ■

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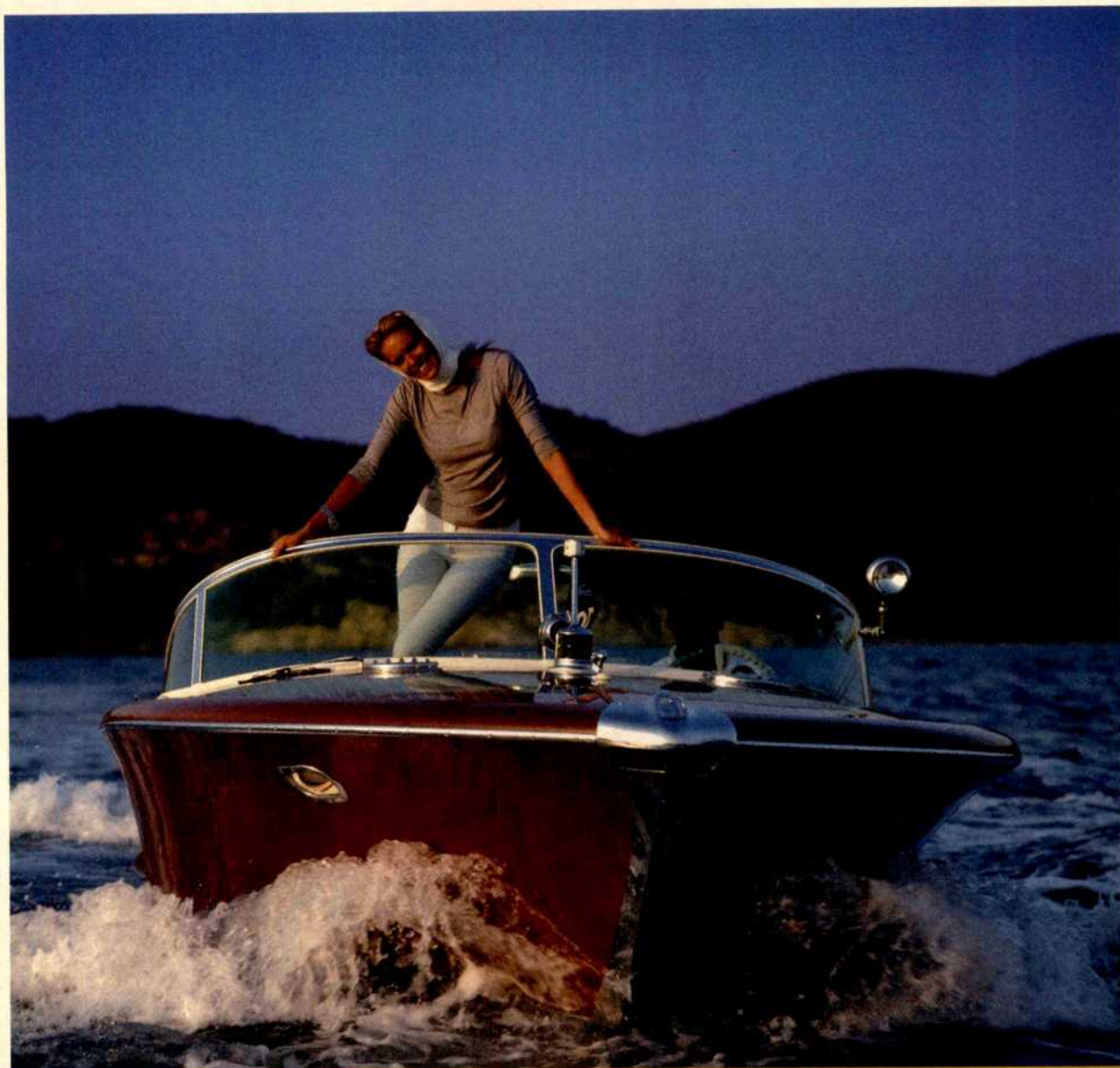
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Airlines

So many planes, so few passengers

Things go from bad to worse for big airlines, and not just because of September 11th

SOON after terrorists destroyed the World Trade Centre using hijacked planes, Ryanair launched an aggressive campaign in doubtful taste. Using a pastiche of a first-world-war recruiting poster with Lord Kitchener's pointing finger, Europe's second-largest low-cost airline proclaimed, "Let's fight back". To strengthen timid hearts, it promised seats for under £10 (\$15). Amazingly, the strategy worked. Passengers flocked to Ryanair and its rival easyJet, which embarked on similar aggressive discounting.

The reaction of the big, established network carriers in Europe and America was quite the opposite: they slashed capacity by 15-20%, anticipating (correctly) a slump in their passenger numbers. Even though they in turn have cut their high fares, their passenger numbers are still running well below pre-September 11th levels. The recovery which started in America in January fizzled out in the early summer, as business travel remained depressed and many corporate "road warriors" were told to fly low-cost or not at all. American carriers, which lost \$6 billion in 2001, look like losing even more this year.

In Europe this week Michael O'Leary, the combative Irish boss of Ryanair, was banging his big drum again, launching a

week-long giveaway of 1m free tickets for flights in the slack fourth quarter of the year. This, he hopes, will end the recent fashion for criticising his airline over lost bags, delayed flights and overworked pilots. But, complaints notwithstanding, the market says he is doing things right.

While British Airways' traffic is down by 10% this summer from year-ago levels, Ryanair's numbers are up by about 40%. Nor does cheap mean profitless. This month British Airways has fallen out of London's FTSE 100 index of leading shares; Ryanair's market capitalisation has long exceeded that of Blighty's flag-carrier.

The same pattern has emerged in America, where the only consistently profitable big airline is Southwest—now worth more than the big six network carriers added together. JetBlue, a small but growing low-cost airline, is also winning rave reviews from American passengers.

The unfriendly skies

Last month, US Airways became the first of the big American carriers to go bankrupt since the post-terrorism government bail-out. United Airlines, still seeking the labour concessions it needs to qualify for a second dollop of federal aid, may soon follow it into Chapter 11 bankruptcy. United

has cash, but is burning it fast. Its biggest problem is that workers own 55% of the firm and, in effect, dominate the board. The employee-shareholding scheme that rescued the airline eight years ago when pilots and other staff traded salary for shares has soured. For all the supposed attractions of worker-owned firms, United's employee-capitalists seem unable to act in their collective long-term interests.

But each of America's network carriers is now into a second phase of adjustment to the crisis. Last year's big cuts in capacity and jobs were not sufficient. With fuel and security costs soaring, and revenues dropping, they are in penny-pinching mode. Service quality is falling. Forget about free drinks and snacks, let alone happy flight crews. In part to encourage cheaper-to-provide direct bookings by phone and Internet, most carriers are now charging \$20 extra for paper tickets. They are tightening conditions on refunds and scrapping corporate discounts on cheap fares.

But bigger changes loom. The essence of what a network carrier offers, through its hub-and-spoke system, is many destinations and frequent flights through connections at hubs. In normal times, this minimises the revenue risk of not filling aircraft. But to ensure slick connections at peak hours for high-fare business travellers, aircraft have to hang around at hubs.

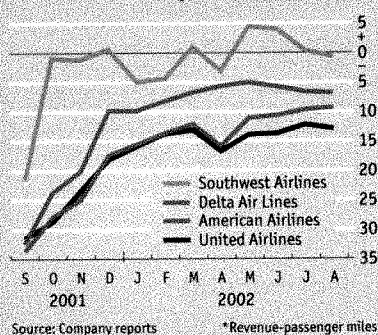
Low-cost point-to-point carriers mostly provide flights between two places, without the swift connections available at a hub—relying on low fares to attract enough business. But they work their aircraft and crews harder. According to Aviation Economics, a London consultancy, low-cost carriers get 11 hours flying per day out of

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Southwest on top

Airline traffic*, % change on a year earlier



► each aircraft, compared with only about nine hours for a network carrier.

Recently, American Airlines, which invented the hub-and-spoke system, has been squeezing more flying hours out of each aircraft by spreading connections over a longer period. Business passengers are no longer willing to pay premium fares for slick connections. So American, closely watched by its rivals, is spreading out its flights in a "rolling hub", holding fewer aircraft on the ground to provide peak-hour connections.

Even so, traditional carriers remain essentially in a different business from their low-cost rivals, because their networks are more complex. And they have all the historical baggage of unions, entrenched working practices and so on. So it is very difficult for a network carrier to reinvent itself as a low-cost carrier.

A plague of low-costs

Trapped between the rampant low-cost carriers and depressed demand, what else can the big European and American carriers do? Mergers face severe antitrust hurdles. United, for instance, was blocked from buying US Airways 14 months ago, and foreign-ownership rules stymied BA's attempts to hook up with KLM of the Netherlands. So United and US Airways are seeking permission to form a marketing alliance to sell seats on each other's flights by sharing flight-designation codes. Also, Delta aims to join up with Northwest and Continental, an allied pair since 1998.

If approved by the American authorities, these alliances could re-shape global aviation. Similar alliances are forming in Europe, where Iberia and BA are close and Air France is in talks with KLM. This Franco-Dutch rapprochement, plus Delta cosying up to Northwest and Continental in America, could lead to the transatlantic partnership of KLM and Northwest being subsumed into the international Skyteam alliance built around Delta and Air France. Privately, most industry leaders believe there will soon be three groups of international allies, led respectively by American, United and Delta on one side of the Atlan-

Airport security in America

Bad answers to a nasty problem

NEW YORK

Who should be responsible for defending airlines against terrorists?

ONE of the lessons from the massive damage caused by the September 11th attacks is that everyone has a stake in aviation security, regardless of whether they choose to fly. A result is that fresh questions are being raised about who should be responsible for providing, and paying for, a service that may cost close to \$10 billion over the next five years in America alone.

Whatever the answer, the current system, despite extra government spending in the past year, is a mess. There was a serious terrorist attempt in December by a man boarding in Paris who packed his shoes with explosives, and in August a woman was picked up carrying a handgun as she transferred from one domestic American flight to another. In America, where concern is greatest, in the first seven months of this year over 200 terminals were evacuated because of security alerts. As part of a nationwide sweep, 110 people (including a pilot) were indicted on September 17th for using false information on applications for jobs in restricted areas of Denver International Airport.

Glaring weaknesses exist in three areas: poor screening of passengers and luggage, porous barriers to facilities and equipment, and vulnerable computer systems. Addressing any of these is a massive task. By the end of the year, for example, machines capable of scanning bombs and plastic explosives in luggage are required to be installed by every major American airport. This equipment is costly (\$750,000 to buy and as much again each year to maintain), large (in excess of 16 feet long), inaccurate (one false alarm for every five bags), and scarce (1,100 units are needed, seven times the number in operation a year ago). For all these reasons, as many as 40 of the country's 429 biggest airports may be

unable to meet the installation deadline. Because all air transport is linked, any gap may undermine the entire network.

One response would be to give airports (and airlines) more room to improvise by freeing them from federal requirements. An economic analysis published by the Federal Reserve Bank of St. Louis challenges this view, concluding that leaving security up to each institution (which was largely the system until late last year) would produce under-investment (which it clearly did). The institution paying the most would involuntarily share the rewards (a "positive externality" in economics-speak) while still suffering from any deficiency in the weakest link.

Given the (still) small likelihood of any component of the system being compromised by a terrorist attack and the ability to free-ride on the efforts of others, the economically rational reaction would be to spend less than the socially desirable amount. A robust system would be likely only if all the participants were forced to act together, as under a federal programme.

A collective approach has its own problems, notably over-investment. As the government will be judged only by safety, not on the cost-effectiveness of transport, subtle expenses may be ignored, says Cletus Coughlin, an economist at the St. Louis Fed. The cost of passenger waiting time may be valued far less by a federal bureaucracy than by a for-profit firm: the use of busy airports could be unduly restricted. The government will also have a monopoly, vulnerable to such flaws as bloated administration, inflexible management and unresponsiveness to data. In short, there may be no foolproof method of ensuring airport security: another gloomy conclusion from the dismal science.

tic, and by BA, Lufthansa and Air France on the other. This will put pressure on smaller European flag-carriers to drop long-haul routes and become mere regional feeders.

Ray Webster, boss of easyJet, reckons that low-cost carriers will take over most intra-European air travel before the end of the decade, with trains providing the main competition. In America, Frederick Reid, president of Delta, said on September 18th that he expected low-cost carriers to double their share of the American market to 40% "in the near future".

Unsurprisingly, Mr Reid also saw a role

for transnational hub-and-spoke operators. The attacks on September 11th may be only partly to blame for the woes of big network airlines. But the way they aggravated the industry's underlying flaws is likely to lead to a widespread re-shaping of it, featuring a polarisation between international networks on the one hand and regional, short-haul, low-cost carriers operating point-to-point on the other. Certainly, any industry that earns a mere 2.9% net margin on sales in the best of times (as airlines did during booming 1997) is long overdue for an overhaul. ■

Women's magazines

In vogue

Why one part of the magazine business is fat and happy

MAGAZINE advertising is in its worst slump for decades. Ad pages are down, rate cards are under pressure and editorial content is being trimmed. So why does the September issue of *American Vogue* run to a staggering 750 pages and weigh over 1.6 kilos? Pick up four such brick-heavy titles to while away a plane journey and you could exceed your handbaggage allowance with magazines alone.

Vogue is not the only doorstopper among the women's glossies this autumn, but it is the most arm-aching. Such is the inch-thick wedge of advertising pages inside this Condé Nast fashion bible that the first article does not appear until page 206. Its handbag-sized sister title, *Glamour*, runs to 326 pages in October, up by 17% from last year. The boom is not limited to America. The number of advertising pages in the October issue of *Glamour's* British version is up by 77% from the same month last year. British *Marie Claire*, from the AOL Time Warner stable, crowns its October cover that this is its biggest issue ever. Its November issue will be 7% longer again.

Contrast this with the once-fat news and business magazines, including (to a degree) *The Economist*, but above all the technology titles. In the first eight months of 2002, the number of ad pages fell by 72% compared with the same period of 2001 at *Red Herring*, and by 46% at *Wired*.

What is going on? Part of the boom is

seasonal. September and October, along with March and April, are always the fattest issues for the fashion magazines. They coincide with the autumn and spring catwalk shows, when the big fashion houses get the chance to display their wares not only through paid advertising but in gushing editorial copy. The New York shows began on September 18th, as soon as London's fashion week ended. A September issue, says Peter Kreisky, a media consultant, serves as a "directory of the fashion industry: nobody wants to be left out."

Some advertisers may be switching from business and news titles to the women's magazines out of fear that their products will be contaminated by association with bad news, which those publications now have in abundance. "I've got a number of advertisers who have told me: don't put me next to negative coverage of the economy," says Jeff Piper, who places ads in the American press for Carat, a media-buying agency. Plainly, not all products transfer neatly from business to fashion titles. But certain items, such as luxury watches, cars or mobile telephones, seem to be as content nestling next to articles entitled "I'm a monster in bed" or "The truth behind the Britney backlash" as they once were amid stories on corporate strategy.

Perhaps the most important reason, however, is the robustness of retail spending amid the general economic downturn.

In particular, women seem to be spending as never before—even the circulation figures at *Vogue*, *Cosmopolitan*, *Glamour* and their sisters are racing ahead. Flick through the glossies and it is not just the luxury-goods houses—which have traditionally supplied the fashion magazines' aspirational allure—that are splashing out. GAP, for instance, a middle-market retailer, occupies 15 full advertising pages in the September issue of *American Vogue*.

For now, the retail-led boom shows no signs of abating. "There are so many huge new temples to fashion being opened, and they need to be promoted," comments Nicholas Coleridge, managing director of Condé Nast UK. Earlier this year, Prada, an Italian fashion house, opened swish new stores in London and New York. Giorgio Armani plans to open 18 new stores this autumn. Until the retail bubble bursts, the more new stores that open, the longer the magazines that flatter them will stay fat. The only trouble for fashionistas will be finding the muscle to carry both the bulging shopping bags and the bulky magazines that inspire their contents. ■

European antitrust policy

Competing visions

Britain is throwing down an antitrust gauntlet to Brussels

"WHY is there only one Monopolies Commission?" goes the old joke. Britain is preparing to have two, as part of a big shake-up of its antitrust policies. The new system, unveiled on September 16th, has uncomfortable implications in Brussels where Mario Monti's competition directorate is under pressure following a series of controversial rulings.

Britain's changes are part of a new Enterprise Bill now doing its final rounds in Parliament before becoming law, probably in November. Pushed by Gordon Brown, Britain's chancellor of the exchequer, the new rules have a clear moralistic streak. Cartels will be criminalised; individual company directors will face prison if caught breaking the rules. The current Competition Commission and the Office of Fair Trading will each gain greater powers to protect whistleblowers and prosecute offending firms.

It is on Britain's new merger policy, however, that most European eyes are focusing. The law will introduce a string of changes. Some are procedural, formalising a hitherto slightly shambolic system. Ministers will no longer be involved in merger decisions, with the Competition Commission itself having the final say. Both agen- ➤



Phew, a plastic bowl on your head is in this year



There is only one Mario Monti

cies will be upgraded—the Commission alone expects to hire around 70 new staff.

But the crucial change is that, in judging whether a merger should go ahead, Britain is shifting away from the analytical approach favoured by the European Commission towards a more American methodology. In the past, the British used an opaque and politically convenient “public interest” test to evaluate proposed mergers. In future, both of its agencies will apply a “significant lessening of competition” test straight from the American rulebooks. (As there is no agreement between the two agencies on exactly how the rules will apply, there is the slightly unsettling prospect of competition between them—much as sometimes occurs in America between the Federal Trade Commission and the Department of Justice.)

The European Commission uses a typically less permissive “market dominance” test, which has led to its rejection of huge deals such as that between GE and Honeywell. But the test, combined with procedural shortcomings, has put Mr Monti in a tight corner. In June, Europe’s top court embarrassed him, throwing out his 1999 blocking of the merger of Airtours and First Choice, two travel firms. Appeals against two controversial blocking decisions are before the courts, with rulings due soon. The gossip is that Mr Monti’s officials have had a mauling from the court. If the case against either deal is thrown out, there will be renewed pressure for far-reaching reforms within the merger unit.

Mr Monti has recently seemed to be responding to criticism. In July, he gave last-minute clearance to a hostile takeover involving two cruise-ship operators. That unexpected decision came about after he had instructed another team of officers to sit in on the work of the officers handling

the case, to act as sceptical arbiters. Long-standing critics, while impressed, suggested this was just the kind of check and balance Brussels has needed all along.

Mr Monti has listened to complaints that he is too removed from his often dictatorial case officers. This month, he appointed Philip Lowe, an experienced British civil servant who has worked in the merger task force, as director-general of the competition unit. Reporting directly to Mr Monti, Mr Lowe’s job is to sharpen up internal management. He is expected to do a thorough job. Whether he can shift competition policy so that there is reasonable prospect of a common European outlook—let alone a global one—is another matter. ■

The rise and fall of Elektrim

Poland last

WARSAW

Another fine mess for Polish capitalism

ASPECTACULAR plunge in the market capitalisation of a once hot stock, amidst evidence of a wholesale failure of corporate governance. Who said Europe’s former communists could not embrace American-style capitalism?

Not long ago, Poland was seen as capitalism’s best hope in the former communist bloc, and privatised Elektrim was the brightest star in the Polish firmament, cherished by patriots who hoped it would be their national champion. In the past week, due in part to the unforeseen consequences of nationalistic “Poland first” policies, the telecoms and power con-

glomerate filed for bankruptcy and fired its management for the umpteenth time.

Those who have watched the company lurch from one debacle to another, forever to be thrown a lifeline at the eleventh hour, know better than to predict its fate. But Elektrim’s three-and-a-half-year roller-coaster ride involving risky acquisitions, chronic legal and financial woes, and last-gasp rescues by foreign partners is probably nearing its end.

Elektrim is a slimmed-down communist-era trading company that became a much-courted potential partner for European telecoms giants after it seized control of Polska Telefonia Cyfrowa (PTC), Central Europe’s largest mobile-phone operator, in 1999. The firm’s downfall is a case study of an east European firm with delusions of grandeur. Awfully ambitious, but perennially strapped for cash, the company tried to play off Deutsche Telekom against Vivendi Universal for control of PTC, only to incur the wrath of both giant multinational suitors in a protracted legal war.

This contributed to Elektrim’s default last December on convertible bonds worth \$440m. While it won a court-brokered reprieve to restructure its debts, disputed ownership claims over controlling shares in PTC hampered the sale of its telecoms assets, prompting it to pull out of a life-saving debt-rescheduling deal. Although the bankruptcy filing may be a ploy to secure partial debt forgiveness, and may have to be withdrawn if the new management wants to strike a deal with a group of bondholders to off-load its telecoms unit, the firm, whose market value slumped to a measly \$23m from a high of \$1.4 billion, is a shadow of its former self.

Indeed Elektrim’s fall from grace is, in many respects, a microcosm of present-day Poland’s: an exciting growth prospect with valuable assets, stymied by poor management and a bunker mentality. Just like left-wing government bigwigs who prefer national champions to foreign capital, the company was determined to become a stand-alone telecoms powerhouse. (Ironically, it was nonetheless run for years by a colourful American boss, Barbara Lundberg.) “Its critical mistake was to think it could build a Polish giant on its own,” says one seasoned observer of corporate Poland.

By the time it came to its senses and realised that it had to relinquish majority control of PTC in order to stay afloat, the telecoms boom had turned to bust, while its two jilted partners, Vivendi and Deutsche Telekom, had their own problems to attend to. Perhaps if Elektrim had taken its governance more seriously it could have improved its lot. Although numerous representatives of minority shareholders sat on the company’s supervisory board, they often seemed to forget whose interests they served. An all too familiar tale. ■

Hershey

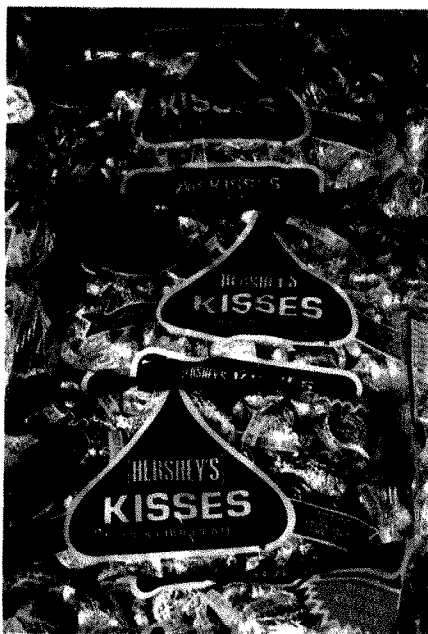
Bitter-sweet

Victory for a company town

NEVER underestimate the power of local politics in small-town America. Hershey Trust is the latest to capitulate before its might, announcing on September 17th the abandonment of its plans to sell its controlling stake in Hershey Foods, America's largest chocolate maker.

The charitable trust, set up in 1905 by Milton Hershey to fund a boarding school for the poor, has almost 60% of its \$5.4 billion of assets tied up in Hershey Foods' shares. While the trustees had been diversifying, and anyway had more than enough money to meet the needs of the school for the foreseeable future, they still felt overly exposed to the fortunes of the chocolate maker. And when a rival food firm—said to be Kraft or Wrigley—inquired about buying the entire stake, they liked the prospect of a juicy premium for their control of the company and a more balanced portfolio.

The trust's sole beneficiary, the Milton Hershey School, is one of America's richest. But even the largest fortune can disappear, especially when undiversified. Minnesota-based Macalester College, once also one of America's wealthiest, learned the value of not putting all its golden eggs in one basket when shares in Reader's Digest, then 60% of its endowment, tanked in 1997. This year the college had to delay sprucing up its dorms and sports facilities.



Maybe not for the trustees

But Hershey's trustees badly underestimated the local outcry when they announced in July their plan to sell. Protesters from the school, the company and former trust members joined residents of the Hershey company town in Pennsylvania—half of whom work for the company—outraged at the risk of lost jobs and of a foreign bidder stripping the town. Enter the state attorney-general, Mike Fisher, an ambitious Republican looking to boost flagging support ahead of the November gubernatorial election. He persuaded the lower courts to slap an injunction preventing the trust from entering into a contract with a bidder without court approval. Curiously, Mr Fisher criticised the trust last year for not diversifying. Insiders claim his chief deputy for charitable trusts, Mark Paccella, advised the trust board to sell Hershey Food's shares—something he denies.

Whatever the rights and wrongs, the trustees have not distinguished themselves. Peter Schoenfeld of PSAM, a hedge fund in New York, is "flabbergasted" that

the trust was so overwhelmed by politics that it acted before an appeals-court ruling, due in days, that was expected to reverse the injunction. Perhaps the trust received advice that gave warning that legal obstacles could take years to overcome. Perhaps the likely buyers, a Nestlé/Cadbury consortium and the favoured Wrigley, demanded that all the legal issues surrounding a deal be resolved first.

The ultimate loser may be Hershey Foods. Although its new management is doing well, the firm is again protected from the risk of unwanted takeover, with all that can mean for dampening incentives and innovation. There may well be missed opportunities—a multinational owner like Nestlé could have taken Hershey's cheap chocolate into big new markets such as China. Hershey itself has never been able to persuade anyone but Americans to eat Hershey Kisses. So there may eventually be reason for the townsfolk of Hershey to regret this week's events. But for now their victory must taste exceedingly sweet. ■

Coffee

Mug shot

Coffee companies prepare for a roasting

ENJOY the last few drops of that grande latte. Soon, thanks to Oxfam, a foe of both poverty and free trade, you might feel too guilty to stomach it. In a new report, Oxfam aims to shame the world's big four coffee sellers (Nestlé, Procter & Gamble, Sara Lee and Kraft) for "impoverishing 25m farmers" in poor countries. The global market for coffee has failed, it says, and needs a complete overhaul (read price controls) so that farmers can get more for their beans.

The plunging price of coffee over the past decade has certainly caused regrettable misery for many farmers. But while Oxfam lays the blame on fat-cat western companies, other forces are more deserving of its ire. New production in Vietnam—partly encouraged by international poverty-relief programmes—combined with vast increases in Brazilian productivity have helped to create a global abundance of coffee. Rich countries' trade barriers make it hard for farmers to switch to other crops.

Solving these problems is not as thrilling as crusading against rich, profitable western firms. Marketers' ability to extract \$4 a cup from middle-class consumers explains why coffee is being lashed by the likes of Oxfam. Its new campaign is cleverly aimed at the anxieties of yuppies—a large proportion of its donors. Oxfam says that coffee farmers are pulling their children out of school.

At the same time, the American television programme "Friends" dares to depict young, attractive New Yorkers sipping cappuccinos at Central Perk without a care. The shame.

Big coffee makers now stand accused of placing profits before people. Though they are probably blameless, expect the prudent ones to fight back by copying big oil companies such as BP and Shell, which cleverly became green-friendly in the face of mounting pro-environment sentiment in rich countries. Already, Nestlé has said that it will support a whole raft of moves to "manage supply"—though not (so far) to start paying all its suppliers higher prices.

Other roasters may well give in to Oxfam's spurious cries, unless they want to gamble with "reputational risk"—ie, having their names tarnished in the media—a huge gamble when a "pure" brand allows you to charge a small fortune for a cup of Java. Far better to use this as a marketing opportunity for "fair trade" coffees—beans for which buyers have agreed to pay over the market price. Starbucks, for one, sells only a little of this type of coffee, but the resulting publicity generates plenty of good customer feelings. Beans with a "fair trade" seal of approval have enabled Cafédirect, a British firm, to turn a small but decent profit; Oxfam even owns 25% of the company's shares.

Business computing

Delete the workers

SAN FRANCISCO

Sun's covert nerd-reduction programme

IF THE number of Elvis impersonators continues to grow at the current rate, it will exceed the earth's human population around 2010, it is said. The nerds in the typical firm's IT support department are proliferating nearly as fast. According to IBM, growing complexity means that the number of IT workers required globally to support a billion people and millions of firms connected via the Internet—possible within the next decade—may be over 200m, two-thirds of America's population.

But fear not. Help is at hand for anybody who fears that their office is about to be swamped by Playstation addicts. It comes in the form of N1, a new sort of über-operating system unveiled on September 19th by Sun Microsystems, a computer maker. N1 will make it much easier to run corporate data centres—thus eliminating much of the work now done by armies of systems administrators.

N1's key concept is "virtualisation"—creating pools of resources such as computing power and storage capacity that can be used as needed. This is done by automating the work of systems administrators. Instead of having to load and configure software manually, they tell N1 to set up a computer system for them—which, assuming it actually works, takes hours rather than weeks. What is more, N1 claims to be self-managing, meaning that it can, say, allocate additional computing resources to a website that faces a sudden surge in demand. Since this means that the many different computer systems in a data centre can easily be re-configured, N1 in effect turns them into one single big system.

To do this, Sun has re-used technology that is already part of its high-end servers and storage systems. This required designing software architecture that is compatible with many different sorts of operating system. But the biggest challenge, says Yousef Khalidi, chief technology officer for N1, was in packaging the technology. It will only be adopted if the nerds who run corporate systems co-operate, which they might not do if it creates too rapid change or even loses them their job.

For this reason, the "virtualisation engine" that Sun will roll out soon will not include features that would scare the more on-the-ball nerds—say, software that automates the process of translating the concept behind a new service, such as online banking, into a computer system. This can wait until the basic system is entrenched.

Shoplifting

While stocks last

PARIS

Thieves versus retailers

WHICH European country boasts the worst record for shoplifting? Step forward Britain, winner of this dubious honour for the second year running, according to a survey released on September 19th. Britons not only steal more than their continental counterparts, they are also less competent employees on the shop floor, resulting in Britain having the worst overall rate of retail "shrinkage"—a measure of losses by retailers from theft, mispricing and other wastage.

Continental Europeans are not much better. Shrinkage is increasing alarmingly in some countries and is generally on the rise. Consider staid Denmark. According to the survey, from the Centre for Retail Research at Nottingham University, shrinkage there is 9% up on last year. Danes remain relatively honest, but are fast closing on their neighbours.

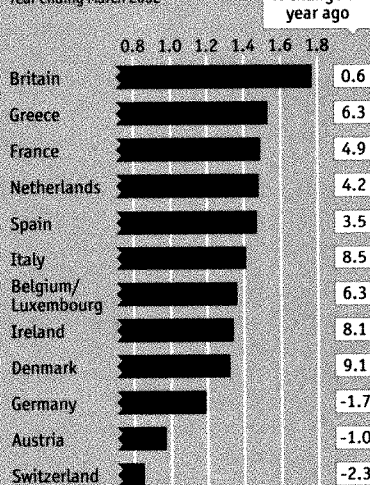
Shrinkage costs the European econ-

omy a surprisingly large amount. Joshua Bamfield, who co-ordinated the study, puts the total annual cost at around €30 billion (\$29 billion) equivalent to a shocking €80 per person in the region. That is more than the costs of the much-higher-profile car crime or domestic burglary. No directly equivalent American survey exists, but a recent poll among 30 of that country's top retailers found they lost an estimated \$5 billion to shoplifting and employee theft in 2001, suggesting the problem there is on a similar scale.

Roughly half the losses in Europe come from theft by customers, who mostly home in on designer goods, electrical knick-knacks and, more bizarrely, vitamins and contraceptives. But almost €8 billion of the theft is by companies' own staff, while suppliers manage to fiddle more than €2 billion from retailers. Even so, it seems that some people still pay when they go shopping.

Light fingers

Shrinkage* as % of turnover
Year ending March 2002



*Loss through crime or wastage
Source: Centre for Retail Research



It is not just Sun's nerds whose future is on the line. Its competitors are working on similar plans. IBM hopes that its eLiza project, part of Big Blue's autonomic computing initiative (see this week's issue of *Technology Quarterly*) will make its huge IT-services arm more efficient. HP intends to build enormous "utility data centres" containing more than 50,000 servers. Microsoft is yet to announce anything specific but has plans for virtualisation software, which will most likely form part of

its Windows operating system.

Sun's established products look increasingly fragile thanks to the creeping commoditisation of its high-end servers and their operating system, Solaris. If N1 is as successful as Solaris, Sun might be able to replicate its current business model on a higher level: just like Solaris, N1 is based on open standards, but works best with pricey Sun gear. If not, Sun may suffer the same fate that it has in store for all those corporate nerds. ■

Face value A helluva problem

The lessons of Jack Welch's outrageous employment contract



GENERAL ELECTRIC has not had it easy since its legendary boss stepped down last year. Yet as if under some abominable curse, Jack Welch seems to grow more virile as GE wilts. The conglomerate's share price sags, yet there is Jack, beaming from the newspaper pages, bouncing about in a noisy, extramarital way with the (now former) editor of the *Harvard Business Review*. There he is again, sporting the same cheeky grin, divorcing his second wife, Jane. Up he pops this week in the editorial pages of the *Wall Street Journal*, trumpeting and justifying his magnanimous refusal of millions of dollars-worth of apartments, private-jet rides, home-entertainment systems and other retirement perks that were due to come his way. At his request, he informs readers, GE has altered his contract, allowing Mr Welch to save the company from the wrath of its shareholders. Another lesson in leadership from the great ex-leader?

Mr Welch has a lot to say about his perks (a "helluva problem") whose size has emerged only thanks to papers filed by his wife during divorce proceedings. Mr Welch's employment contract dates back to 1996, when GE's board was anxious to press millions of dollars into his hands so that he would stay until his retirement at 65. Shocked by the wastefulness of this proposal, Mr Welch suggested that he be paid in kind, in post-retirement perks at (he says) less cost to the firm. There is a danger, he concedes, that by giving up these benefits, it will now seem as if he thinks something was wrong with these arrangements. But for the record, he insists, neither he nor GE behaved improperly, as all was disclosed to shareholders. Is he right?

One measure of how well Mr Welch disclosed his perks can be found at The Corporate Library, a website that keeps an eye on job contracts. Nell Minow, a corporate-governance activist who

created the site, thought back in 1999 that Mr Welch's contract was "a tribute to Mr Welch and his board", guaranteeing no special bonuses, payments or perks. Ms Minow's only worry then was "some vague language in section five, which assures Mr Welch of 'continued access to company facilities and services comparable to those provided to him prior to his retirement, including access to company aircraft, cars, office, apartments, and financial-planning services'."

It was via this language that GE had been planning to dish out, on Mr Welch's estimates, between \$2m and \$2.5m of perks a year. Ms Minow understandably feels misled. The Securities and Exchange Commission is also looking into the adequacy of this disclosure.

Basic instinct

Whether or not GE's actions are found to be improper, Mr Welch's celebrated gut instincts are certainly sending him the right message now. It is proper, even desirable, for bosses who make their firm's shareholders much wealthier—as Mr Welch did spectacularly—to be handsomely rewarded. But it is crucial that they be paid in ways that are transparent to shareholders, and show clearly that the firm is being run in their interests and not those of the boss. This may, as Mr Welch recognised, mean that the company has to pay in a way that is less tax-efficient. But that is worth doing so that the boss, like Caesar's wife, can remain above suspicion—as GE is now discovering.

As questions were raised this year about the quality of its accounts, GE mounted a formidable publicity campaign to put clear water between itself and clearly dissembling firms such as Tyco, a distressed conglomerate whose boss, Dennis Kozlowski, faces an assortment of criminal charges and who enjoyed countless perks from his employer. Mr Welch's perks could easily give the impression, no doubt unfairly, that he, too, has been living it up on his old firm's payroll. And, if that, some investors wonder, what else?

There are other bosses with generous contracts who would do well to follow Mr Welch's lead. Robert Nardelli, whom Mr Welch passed over for GE's top job, now runs Home Depot. His five-year contract there includes a \$10m loan, to be forgiven (what sort of loan is that?) in \$2m tranches over five years; bonuses, options

and deferred stock in vast amounts; an automobile "similar in class to that of the current Mercedes Benz S600"; and a guaranteed minimum payment of \$2.25m a year after he retires. You can almost hear his lawyer (kindly paid for by Home Depot) chuckling to himself.

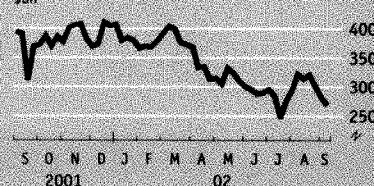
There is no particular reason to pick on Mr Nardelli, although his GE provenance does suggest an interesting pattern. If Carly Fiorina, boss of HP, were in future to be sacked for mere incompetence, massive contractual payments would be triggered. Robert Annunziata, a former boss at Global Crossing, a bankrupt telecoms company, got first-class flights for his mum written into his contract. And so on.

America once worshipped these people as gods, laying offerings of unimaginable wealth—and whatever else they asked for, it seems—at their feet. Now impoverished shareholders are choking on their own disgust. Stern moralists, such as William McDonough, president of the Federal Reserve Bank of New York, are urging restraint in the boardroom. Warren Buffett, the famous investor, chastises greed. Moreover, the cops have woken up, and some once-celebrated bosses are sure to go to jail.

Mr Welch once liked to brag about his supine board, as if it were yet more evidence of his abilities. Yet even boards now sense change is afoot. So do those sleeping giants, the big investing institutions which are meant to fight for shareholders. Cynics talk of market cycles and a return, soon enough, to the old ways. But this convulsion feels too powerful to permit the survival of the *ancien régime*. It is not ignoble and sanctimonious moral disgust that will seal its fate. Much more powerful is the pervasive sense of foolishness. Mr Welch, more than most, deserved to be well rewarded. But as he himself has come to realise, giving some back "sure feels right in my gut". ■

Unhappy retirement

GE's market capitalisation since Jack Welch retired \$bn



Source: Thomson Datastream

1st Semester Consolidated Result Highlights

January 1st - June 30th

	June 2002 (Audited)	June 2001 (Audited)
Profit After Tax ¹⁾	Rp 1.77 trillion (US\$ 202.52 million)	Rp 1.13 trillion (US\$ 99.13 million)
Return on Assets - before tax	2.3% p.a	1.2% p.a
Return on Equity	27.6% p.a	15.8% p.a
Capital Adequacy Ratio - Bank Only	29.8%	28.5%
Non Performing Loans Ratio ²⁾	9.2%	14.1%
Net Interest Margin	2.7% p.a	2.9% p.a
Cost Efficiency Ratio ³⁾	41.0%	33.4%

Notes :

1) Based on exchange rate June, 30 2002 : 1 USD = Rp 8,740 ; June, 30 2001 : 1 USD = Rp 11,440

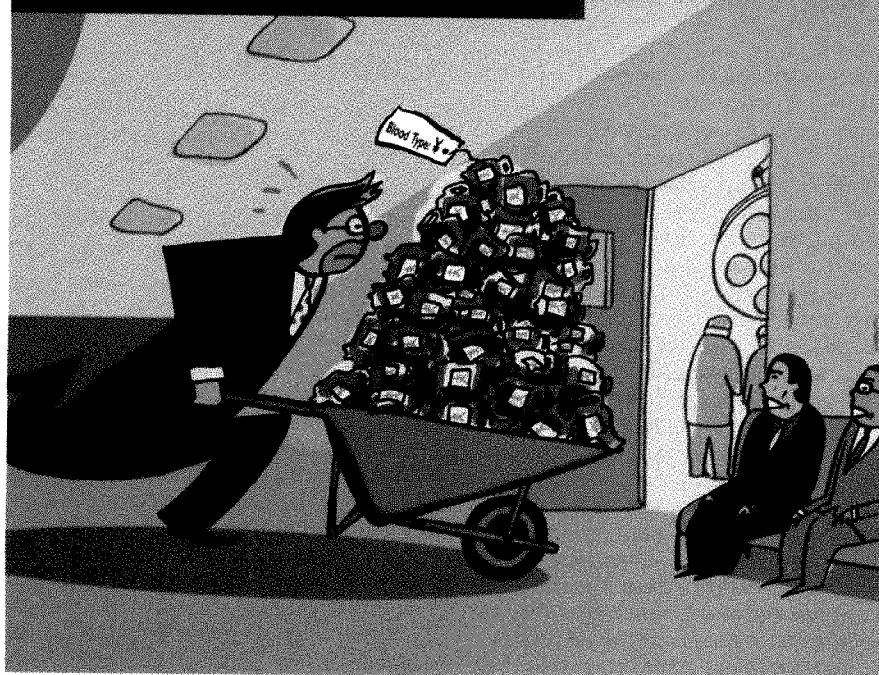
2) Non Performing Loan to Total Loans

3) Overhead Expenses/Net Interest Income, Commission and Fees income and Other Operating Income (exclude gain on foreign exchange transactions and gain from increase in value and sale of securities and government bond)

"During the period between June 2001 - June 2002, we enhanced our products and services, information technology platform and distribution network as part of our corporate strategy of extending our leading position in Indonesia".



E.C.W Neloe
CEO, Bank Mandiri



Bank of Japan

Shareholder of last resort

TOKYO

Japan's central bank steps in to support banks' share portfolios

COULD this, at last, be an official admission that Japan's banks are on the brink? Many wonder what, besides deep and possibly imminent trouble, could have prompted the statement from Masaru Hayami, the governor of the Bank of Japan (BOJ), on September 18th, that it plans to buy shares directly from banks in a bid to stabilise the financial system.

By helping banks reduce their huge equity portfolios, already loaded with losses, the central bank says it hopes to shield them from further falls in an equity market which earlier this month hit a new 19-year low. Reducing such risks, which remain "a significant destabilising factor" for the banking system, it insisted, was an "urgent task".

It was an unexpected about-face by a central bank which had, until almost the day before, stubbornly resisted pressure from ministers and politicians to prop up the stockmarket or bail out the banks. It was also a reversal of the BOJ's long-held view that buying equities is part of fiscal policy and therefore not in its mandate. (In fact, the central bank needed permission from the Ministry of Finance—permission that was immediately granted.)

Mr Hayami's bombshell, bursting just before the Tokyo Stock Exchange closed for the day, put the markets in a last-minute frenzy. The benchmark Nikkei 225, which

had been falling steadily all day, shot up more than 200 points, to just short of 9,500. The rise was matched by equally swift falls in the bond and currency markets: investors feared that the move would damage the BOJ's fragile balance sheet, and that its volume of bond purchases might fall. The ten-year government-bond futures contract suffered its biggest daily fall in two years, while the yen dropped to a three-month low against the dollar.

After this excitement came questions—but few answers. The central bank merely said that it wanted to start buying shares as soon as possible, at market prices, and hold them for at least ten years. But how much does it want to buy? The big banks hold about ¥24 trillion (\$200 billion) of equities; recent regulatory changes require them to reduce this to the level of their tier-1 capital, currently ¥17 trillion, by September 2004. The central bank may intend to take the balance off their hands. But the terms and conditions of the purchase are still being worked out.

Yasuhisa Shiozaki, a politician in the ruling Liberal Democratic Party (LDP), wonders why the BOJ would use "a measure of last resort" when the role of ensuring that the banking system is sound lies primarily with the Financial Services Agency (FSA), the bank regulator. Others wonder whether the central bank, which

has for years pushed the government (with little success) to speed up the disposal of the ¥150 trillion of bad debts in the banking system, is hoping to prod it into action. But that would require a big change of view at the FSA, which continues to insist that the banks are fine.

So far the central bank has not linked its planned bail-out to any quid pro quo from the government in the form of more fundamental reforms to clean up the banks. Yet surely, says Kohei Otsuka, a politician in the Democratic Party, if the Bank of Japan believes that the banking system is so weak that it requires such desperate measures, it should be pushing for broad, drastic solutions, including, perhaps, temporarily nationalising banks while they are being cleaned up.

The Bank risks losing credibility if its strategy backfires, warns Koyo Ozeki, a credit analyst at Merrill Lynch. By transferring risk assets, which by its own admission could fall in value in the coming months, it could take big losses itself. Furthermore, says Garry Evans, a strategist at HSBC Securities, the taboo of buying equities, once broken, could become a habit, reinforcing the belief that the authorities will always step in when the equity market falls to a certain level.

Worse, the BOJ's jealously-guarded independence is now in doubt. Many already believe it has bowed to political pressure. Such concerns could trigger further falls in the currency and government-bond markets, in turn creating big losses in the commercial banks' huge bond portfolios and eroding their capital—the very outcome that the BOJ set out to avoid.

The central bank is staking a great deal on a measure that may do little more than temporarily bolster the stockmarket. The ►►

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BOJ insists that this is not part of the LDP's regular efforts to prop up the stockmarket before banks close their financial books at the end of March and September. Yet the plan is unlikely to provide any profits for banks to use to write off bad loans: they almost certainly bought most of these shares when prices were higher.

Why don't the banks simply sell their shares directly into the market, or to the special stock-buying entity recently set up by the government to help them unwind their cross-shareholdings (which the banks dislike because of the strict reserve requirements attached to them)? The only new twist offered by the latest plan is that it avoids putting downward pressure on the stockmarket—a sign, says Mr Evans, that the central bank has indeed been co-opted into the LDP's latest price-preserving operations. ■

Asset-backed securities

Go with the flow

NEW YORK

Fall-out from financial scandal threatens a crucial debt market

THE collateral damage from America's campaign against corporate corruption is still spreading. A new source of concern is "The Employee Abuse Prevention Act of 2002", a virtuous-sounding bill bouncing around Congress that could undermine the legal foundation of the trillion-dollar asset-backed securities market. Asset-backed finance, for all its flaws, plays a huge role in reducing the borrowing costs of American corporations, and of the average citizen too.

The most damaging changes sound well-intended and innocuous. Under the bill, sponsored by a consortium of Democrats led by Senator Dick Durbin of Illinois and Congressman Bill Delahunt of Massachusetts, the federal bankruptcy law would be tweaked to allow the court to "recharacterise" certain kinds of debt as well as the position of creditors. Typically, with asset-backed deals, companies promise to divert assets or cashflow from a part of their business (such as credit cards or car loans) into "special-purpose" entities—legally distinct companies that raise money through the sale of bonds. The bondholders receive the value of the securities at maturity on the basis of these designated cashflows, regardless of what happens to the parent company—and even if the transfer of assets eats into resources that are needed to fund pensions and maintain employment.

The purpose of the bill, says Mr Durbin, is to ensure that "the forgotten victims—

employees and retirees—won't be asked to pay the price" of "an epidemic of corporate greed and corruption." The best argument in favour of the Durbin-Delahunt position can be summarised in one word: Enron. The energy giant had an affection for these special vehicles and, allegedly, used them not only to disguise its true financial condition, but also to channel wealth to a small group of its executives.

But that should not disqualify the product altogether. Undermining the independence of special-purpose vehicles could raise the cost of borrowing for any business in the lower credit range—that is to say, much of corporate America.

Asset-backed borrowing first became popular in the early 20th century when even troubled railway companies found they could finance their rolling stock cheaply as long as the loans were secured on the wagons themselves. The same technique has allowed America's troubled car rental firms to finance at the same rates as strong investment-grade companies. A decade ago, the asset-backed market covered only a handful of areas, primarily debt tied to homes, credit cards and cars. Moody's now rates securities backed by over 90 kinds of assets and cashflows, including mutual-fund commissions and tobacco-settlement payments.

But there have been glitches. Moody's has examined disasters during the past four years to illustrate that the early optimism about the market was vastly overblown. The asset-backed structure does poorly when the parent company is small, with no other sources of financing, and if it is involved in a fringe business, such as dodgy car loans or poor credit-card debt.

Then there is the reliability of a guarantee. A crucial failure occurred when AIG, a big insurance company, was perceived to have provided a guarantee for an asset-backed film deal, and then pulled out, precipitating the default of a highly-rated security. The market has since got wiser.

A change in the law is a bigger threat than corporate failure. If the special-purpose vehicle is not considered distinct from the parent company, its financing advantages will be lost. Before the Durbin-Delahunt bill, the biggest test came in December 2000, when LTV, a steel company, filed for bankruptcy and tried to retain money it received on inventory and receivables that it had already in effect sold to two special-purpose vehicles for \$650m. The money was badly needed; nearly 20,000 jobs were at stake.

A local judge gave a preliminary ruling in LTV's favour. In response, a consortium of large banks, terrified of the impact of an adverse decision on the broader asset-backed market, arranged a complex bailout that failed to save the company, but preserved the financing structure, at least for the moment. ■

Euro-area economies

Catch 2002

FRANKFURT

As stockmarkets plunge, strains also show in the EU's stability pact

A FEW months ago, economists were forecasting steady recovery for the euro area. Oops. The zone's economy grew by only 0.4% in the first quarter and 0.3% in the second; the third is looking bad too. This week came news of a sharp fall in French industrial production in July and a rise in euro-zone inflation to 2.1% in August, above the goal of the European Central Bank (ECB). The bank, no softie anyway, is now less likely to cut interest rates. Europe's equity markets, already battered by global gloom, slumped. Germany's blue-chip Dax 30 index dropped 5% on September 18th, hitting a five-and-a-half-year low, and France's CAC 40 fell by 3.6%.

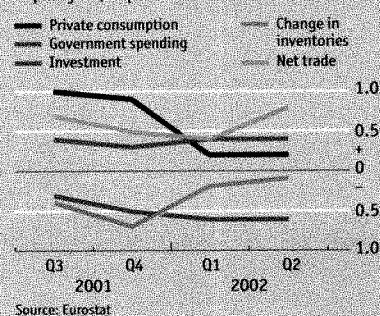
Slow growth has not only caught out the pundits: it is straining the euro-area's budgetary rules, the "stability and growth pact". The idea of the pact is to prevent governments running loose fiscal policies at the expense of other euro-area countries. This could happen through higher interest rates if the ECB offset fiscal laxity with tighter monetary policy; or by a higher risk premium on euro-area government bonds.

The Maastricht treaty, which laid down the rules for euro membership, says that governments may not have budget deficits of more than 3% of GDP, except in a "severe economic downturn", defined as a drop in GDP of more than 2% in a year, or when some other "unusual event" blights their finances. On top of this, governments are supposed to keep their budgets near to balance, allowing for cyclical fluctuations.

Four of the 12 euro-area governments—the three biggest, Germany, France and Italy, plus little Portugal—are off target. Earlier this year, they promised to bring their budgets "close to balance" by 2004. But the laggards are being pushed away from bal- ▶▶

Trouble at home

Euro area, contributions to change in GDP in past year, % points



ance in 2004, not towards it, and they do not seem to care. Germany, in effect, is aiming for 2006. France's commitment to 2004 is conditional on economic growth of 3% in 2003, which looks out of reach. Moreover, its finance minister wants to cut taxes. So does Italy's. The Italian deficit, despite an official forecast of 1.1% for 2002, will probably be well over 2% both this year and next.

Letting the 2004 deadline slip makes sense. For a year or more, the euro area has been suffering from chronic weakness in domestic demand. Consumer spending is feeble in Germany and Italy; it is stronger in France, but could be weakened there by rising unemployment. Investment has also been frail: its weakness in the second quarter of this year cancelled out slightly perkier consumption. In effect, net exports have kept the euro economy going. Tighter fiscal policy may be the only way of hitting the 2004 target. Yet, with demand so weak, it is the last thing the euro area needs.

The sacred 3% limit for budget deficits, already burst by Portugal last year, will probably be breached by Germany this year. Weak economic growth could tip France over in 2003. Transgression can have dire consequences. The European Union's finance ministers are supposed to make recommendations intended to wipe out the excess deficit the year after its discovery. If the offending government does not comply, it has to lodge a deposit, at zero interest, of between 0.2% and 0.5% of GDP with the European Commission. If the sin is not corrected within two years, the deposit is converted to a fine.

Italy would like the pact to be eased. The French and German governments surely would too, though they are less vocal about it. The ECB, however, growls at any sign of weakness. Wim Duisenberg, its president, said recently that "countries with remaining imbalances must avoid deficits in excess of 3% of GDP and implement determined policies in order to progress towards budgets close to balance or in surplus."

David Walton, an economist at Goldman Sachs, says that the pact aims at the wrong thing. It makes no sense, he says, for all the euro area's governments to aim at budget balance no matter how much debt they carry. A rule intended to stabilise government debt at 60% of GDP, one of the Maastricht criteria for joining the euro, would allow most governments (but not Italy's, a big debtor) to run a small deficit most of the time and permit occasional deficits of more than 3%. Mr Walton thinks that this could be done without changing the treaty.

But would it help? Markets might see an easing of the pact, daft as it is, as a sign that ministers have no real interest in balancing their books. So delinquent countries would be punished either way. ■

Asbestos litigation

Spreading out of control

NEW YORK

American asbestos litigation is in need of change

ABOUT 8,000 people claiming exposure to asbestos are suing 250 companies, including Mobil and Honeywell, in a trial starting in West Virginia on September 23rd. Many of these people are "unimpaired"—they show signs of asbestos exposure but are not actually sick. If a settlement is reached between the defendant companies and the plaintiffs, the unimpaired will be compensated (for their anxieties) as well as the critically ill. That would eat into the share of compensation going to the actual victims of asbestosis, a progressive scarring of the lung tissue that makes it hard to breathe, or of mesothelioma, a nasty form of lung cancer.

The unfairness of this is the chief argument used by companies defending themselves against mass litigation in asbestos lawsuits. There are some 200,000 asbestos claims currently pending in America, about a third of all those filed since the first lawsuit in 1966 in Beaumont, Texas. The legal system is clogged with them, but estimates for the final number of complaints range from 1.1m to 2.5m.

Today's claims are different from the first ones more than three decades ago. According to the RAND Institute for Civil Justice, a think-tank in California, about two-thirds of the claims are now filed by the unimpaired, while in the past they were filed by only the manifestly ill. And with most manufacturers of asbestos already bankrupt, the companies now taken to court are those that played a peripheral role, such as transporting the stuff or using minimal amounts in their products. Claimants among the "worried well" are lured by advertisements and by lawyers promising them money, says Steven Kazan, a lawyer who defends only the critically ill.

For insurance companies, another avalanche of multi-million-dollar claims from companies losing such cases could hardly come at a worse time. At the same time as their investment returns were plummeting last year, they had to cope with unusually high claims for natural catastrophes as well as the largest insured losses ever from the terrorist attacks of September 11th. But asbestos could yet result in bigger pay-outs than the combined losses from Hurricane Andrew, the costliest natural disaster to date, and the attacks on the World Trade Centre. Tillinghast-Towers Perrin, a consultancy, estimates that insurers will be stuck with about a third of the \$200 billion final bill for asbestos. Last week, after a



A \$200 billion business

study by Tillinghast on the asbestos liabilities of Fireman's Fund Insurance, its parent, Allianz, added \$750m to the company's asbestos reserves.

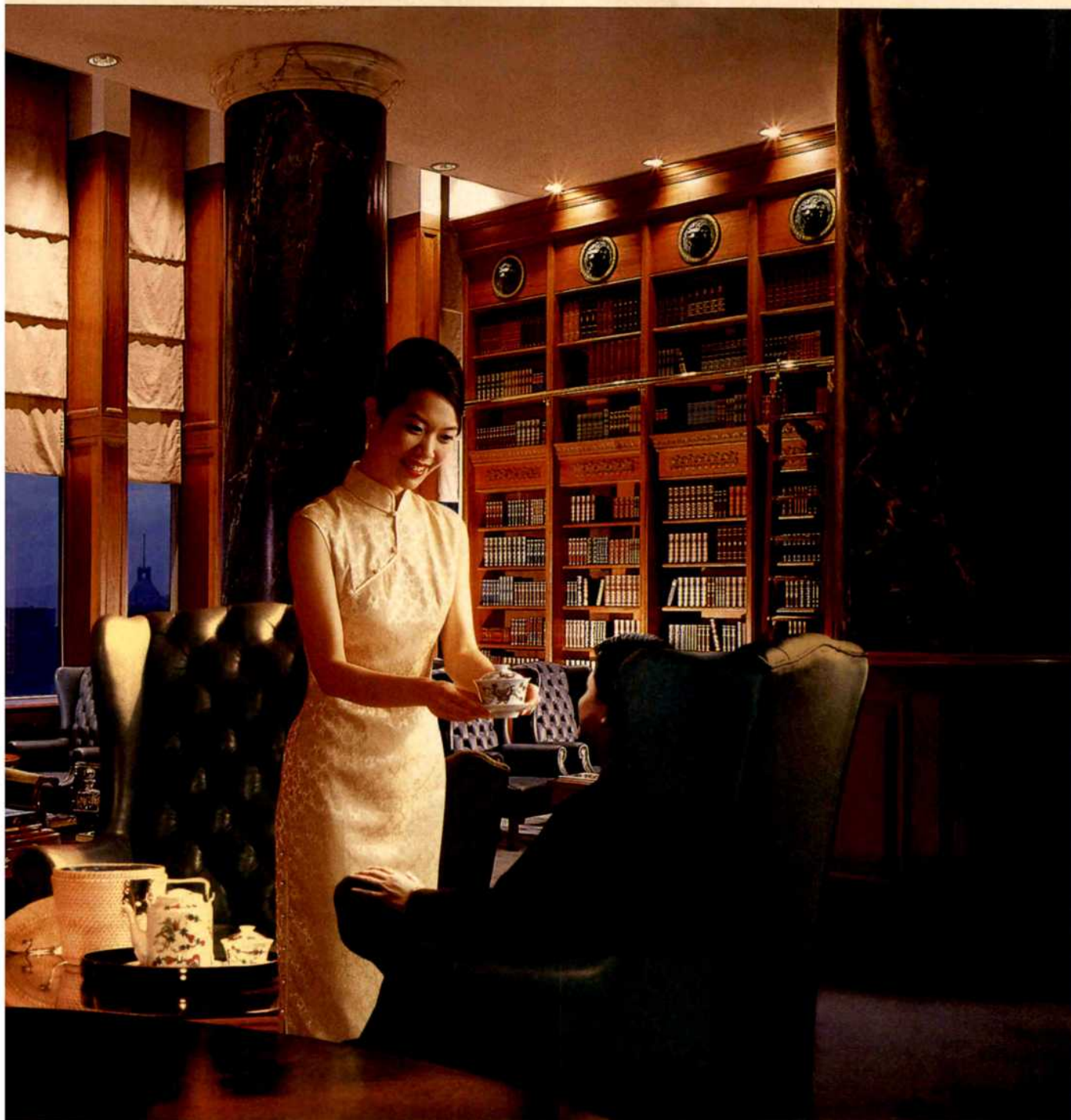
At the end of last year, Berkshire Hathaway added 30% more to its asbestos reserves of \$6.3 billion and CNA Financial doubled its asbestos reserves to \$1.2 billion. Some insurers try to settle quickly, once and for all, even at high cost. St Paul paid nearly \$1 billion in June to settle a single asbestos claim by Western Asbestos. In May, a dozen insurers settled with PPG Industries, a chemicals and paint manufacturer with a half-share in an asbestos producer, for \$2.7 billion to resolve all current and future claims.

At the same time, insurers are stepping up their campaign for new regulation and legislation to rein in asbestos claims. They would like to establish objective medical criteria for claimants, remove incentives to file claims without a manifest injury, ban consolidated claims, and bar attorneys from filing their claims in states that have no connection with the case. Evidence of asbestos injury, apart from mesothelioma and asbestosis, is heavily contestable. Shadows on x-rays could also be caused by smoking or pollution. "The reading of x-rays is very subjective," says James Foster at Everest Re. Individuals react differently to asbestos. Some women die of me- ▶▶



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sothelioma, because of having washed clothes exposed to asbestos, but an asbestos insulator in Montana is 85 today and still hiking in the mountains, says Gregory Munro at the University of Montana.

Insurers are lobbying to end consolidated claims (trying thousands of cases at once) and "forum-shopping", whereby lawyers choose the most favourable jurisdiction. Tort law varies considerably from state to state. Only West Virginia and Mississippi allow litigation by very large numbers of claimants, as in the trial starting next week. Trial lawyers have been deluging courts in these two states. One county in Mississippi has 21,000 asbestos cases but only 9,700 inhabitants.

Insurers and a handful of trial lawyers, such as Mr Kazan, have united in a common cause: to get Congressional action to discourage the absurdities outlined above. But until now reform has repeatedly been blocked by the Association of Trial Lawyers of America, a powerful lobby that is one of the biggest donors to the Democratic Party and to law schools—deans of

American law schools are hence not great fans of tort reform.

The majority of asbestos cases are settled out of court, points out Fred Baron, a lawyer at Baron & Budd, America's largest asbestos-law firm. But there are plenty of asbestos cases still coming to court—which is an inefficient use of resources. Litigation eats up 60% of the money spent on asbestos claims, says Philip Howard, a lawyer and a fierce critic of America's law-suit culture. He proposes taking asbestos claims away from the tort system by creating a federal scheme to compensate those who are really sick.

But who would pay? Federal schemes are expensive and create bureaucracy. Taxpayers are unlikely to applaud a bail-out of insurers and corporations, some of which were well aware of asbestos dangers at an early stage. The Senate Judiciary Committee will hold hearings to re-examine the issues surrounding asbestos liability on September 25th. But after 20 years of inaction, the chances that they will lead to effective change are small. ■

Fair disclosure

Share and share alike?

In Britain, some shareholders are more equal than others

BRITISH punters may have thought that their stockmarket was based on the bedrock principles of fair play. They like the idea that all shareholders are treated equally. Yet, despite the fact that its rules forbid giving some shareholders more information than others, there have often been breaches in practice.

That is just the kind of thing America's Securities and Exchange Commission was aiming to stamp out when it created Regulation Fair Disclosure (FD) two years ago, with heaps of new laws to ensure proper disclosure of "material information". But some in London are now wondering whether too much equality is a good thing. And they are finally working on changes that may end the wink-and-a-nod breaches that have plagued the principle in the past.

Of course, having the same information will hardly make shareholders equal. Some will take a keener interest in it than others. Most will have little means or motivation to keep a close eye on management. Even the big shareholders fall down on their watch. Which big money manager, for example, spotted Enron's or WorldCom's failings before they became public? Moreover, the easiest way for an investor to protest to management is not to sign up for the costly process of shareholder meetings and proxy votes, but simply to sell the shares of companies which are not quite up to scratch. For Britain's small investors, walking away from a company's shares is the best way to make their displeasure felt. ►►

Chapter 11

In trusts we trust

NEW YORK

Companies with large asbestos liabilities are seeking shelter in bankruptcy

BANKRUPTCY may not sound like an attractive option, but it is often the best alternative for firms in the throes of asbestos litigation. Ten asbestos-exposed firms have filed for bankruptcy so far this year, up from nine in 2001. Johns-Manville, a building-products firm that was one of the first asbestos-related bankruptcies when it filed for Chapter 11 protection in 1982, pioneered a process under which bankrupt firms segregate their asbestos liabilities in a trust. The trust absorbs all past and future asbestos responsibility, clearing the way for a clean reorganisation of the company.

In return, the trust receives monies for payments to asbestos claimants in the form of cash, stock, insurance policies and profit-sharing plans—the Manville Trust received 20% of Johns-Manville's consolidated profits until the firm was sold to Berkshire Hathaway in 2001. Trusts also have majority voting power in the new, cleaned-up firm. And companies receive a tax deduction on all payments that they make into the trust.

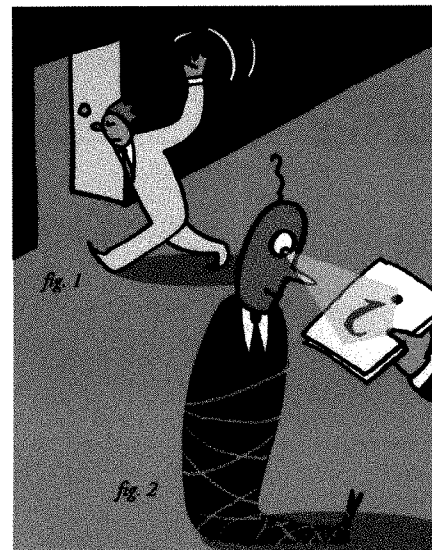
The Manville approach is catching on. Skyrocketing asbestos claims are pushing more and more companies into the red: National Gypsum, which filed for Chapter 11 in 1990, is establishing a Manville-like trust this year. Babcock & Wilcox, a bankrupt boilermaker, and PPG Industries, parent of the bankrupt

Pittsburgh Corning, are doing the same.

But Manville is not a panacea: trusts only shift around the onus of asbestos liability. Since 1988, the Manville Trust has doled out \$2.7 billion to approximately 443,000 claimants, but it still receives 8,000 to 10,000 new claims per month, according to Robert Falise, its managing trustee.

Babcock & Wilcox is hoping to change the dynamics of the game, in an effort to reduce the burden of claims. It is pursuing a strategy of sorting valid, scientifically-based claims from frivolous ones by having claimants fill in forms detailing their asbestos-related personal injuries, medical diagnosis and work record. More controversial still, the company is pushing for outside experts to address the scientific basis of asbestos claims in court. W.R. Grace and Federal Mogul, both bankrupted by asbestos liabilities, have filed briefs based on Babcock & Wilcox's approach.

Norfolk & Western Railroad is taking another slant. It challenged a \$5.8m jury award granted to six healthy railroad workers who claimed emotional distress caused by fear that they might possibly develop cancer from past exposure to asbestos. In April, the Supreme Court agreed to hear the case, raising some hope that limits might be imposed on future claims.



Nowadays, however, over half of Britain's equity markets are owned by institutional shareholders, such as pension funds and life insurers. Some of these institutions, responding to complaints of apathy in the face of corporate malfeasance, have strong ideas about how companies should be run and enough shares to make those ideas stick. They have been able to bend the ears of the chief executives, asking and receiving information that less important shareholders might not be able to hear.

Technically, however, such selective briefing can fall foul of the Financial Services Authority (FSA), with its strict insistence on a blunt principle of equality of information. The cost is likely to be a dumbing down of communication with the market. If managers cannot have a private chat with influential shareholders without also telling the whole street, company bosses are more likely to keep mum on big questions of strategy. Ken Rushton, Director of Listings at the FSA, says that under the current rules, lawyers are advising managers: "If in doubt, shut up".

Even with America's detailed rules, its experience in the years since enacting Regulation FD shows how hard it is for financial regulators to spot a breach of the rules. FD was designed to prevent corporations from sharing key information with some analysts and investors, while keeping everyone else in the dark. It has encouraged managers to take advantage of such tools as webcasting open teleconferences to reach widely scattered shareholders.

Yet for all its radical egalitarianism, Regulation FD has never been as draconian as it looks. In fact, it does allow for some exceptions: specifically, inside information can be shared with someone who keeps it to himself and does not use it to profit from share sales. Now the FSA is contemplating something similar, if only to keep up with practices which have long been acceptable among City analysts and big institutions.

The FSA's idea is to permit managers to invite chosen shareholders to take on the status of corporate "insiders". As temporary insiders, these shareholders will be able to hear confidential information about strategy, and tell the managers just what they think. But there is a price for this forbidden knowledge and power: they forego the right to trade the company's shares for a while, until their inside information becomes public knowledge.

But will institutional investors accept the invitation to participate in corporate governance? Fat chance. Mr Rushton admits that it is not the institutional shareholders themselves who have sought to broaden the rules. Many investors would sooner cut off their ears than risk hearing anything that would restrict their freedom to trade. Walking, for British punters, may be rather cheaper than talking. ■

Corruption in Lesotho

Small place, big wave

JOHANNESBURG

A conviction for bribery could have a wide impact

TURN on a tap in Johannesburg: the crystal clear water that fills your glass has travelled some 300km from a dam in neighbouring Lesotho. The little mountain kingdom earns foreign currency exporting water from an \$8 billion irrigation system: the Lesotho Highlands Water Project, one of the biggest constructions in Africa. But waves from the dam are spreading beyond Africa's shores. This week, a Canadian company which helped build the dam was convicted of paying bribes in a corruption case that could change the way big development deals are struck.

On September 17th, a Lesotho court found Acres International, a Toronto-based firm, guilty of passing \$260,000 as a bribe to the chief executive of the project, Masupha Sole. In June, Mr Sole was convicted of 13 counts of bribery and of accepting more than \$2m. He was told he would serve 18 years of a 57-year prison sentence. Even if an appeal by Acres fails, no member of the company will go to jail after sentencing in early October, but a hefty fine is likely. More threatening is the impact of the conviction on Acres's other building activities.

The company is involved in two more dams, in Uganda and Laos, which are expected to receive World Bank funding, and it has helped build enormous reservoirs such as the Three Gorges Dam in China. This week, an official at the World Bank said it had learned of the conviction of Acres and would "now determine whether further action by the Bank is warranted to exclude the company from future bids." Since 1999, the Bank has promised to bar any company from development

projects if it is found to be involved in corruption. Over 70 companies and individuals have been excluded so far. A Bank committee which conducted a two-year investigation into Acres International, but found no evidence of wrongdoing, is expected to reopen its case soon.

Legal proceedings are also underway in Lesotho against some of Europe's biggest building companies, which were also involved in the consortium that built the dam: Lahmeyer International of Germany, Britain's Balfour Beatty and France's Spie Batignolles and Dumez International. Anti-sleaze and anti-dam activists demanded this week that the Bank crack down on corruption by barring all these companies from other lucrative contracts if they are convicted.

The World Bank is also under pressure to make big aid projects more effective and less corruption-prone. Last December, its own Operations Evaluation Department said that the institution's activity in Lesotho had been "moderately unsatisfactory"—harsh words indeed from an internal report—and suggested that the Bank avoid big building projects and focus instead on poverty alleviation, education and health.

On September 18th, the African Union said it too would ratchet up efforts against graft, which it guesses costs the continent nearly \$150 billion a year by increasing the price of goods. While officials are often to blame, the Lesotho government hopes the new conviction will change the image of African governments as being hopelessly corrupt. Guido Penzhorn, an advocate who led the government team, argues that the case is important because it highlights the damaging role of those who offer bribes: "This turns on its head the perception in first-world countries that consultants are obliged to pay bribes in Africa. It was the company that offered money; it is very important that the briber was convicted. People here are very aggrieved when the rich world writes this off as just an African problem." ■



Pure source of corruption

Economics focus Treading lightly

Does mankind need more than one planet?

IN THE discussions surrounding last month's United Nations World Summit on Sustainable Development, a particular measure of environmental stress was often cited—mankind's "ecological footprint". The idea is to translate human demands on the environment into a common unit, so they can be added up. The footprint is the physical area required to meet man's needs and wants. This can be compared with the productive area available, to give a sense of how sustainable those needs and wants may be.

In its *Living Planet Report 2002*, WWF, a conservation group, says that mankind's ecological footprint is already 1.2 Earths. "Humans are currently running a huge deficit...using over 20% more natural resources each year than can be regenerated, and this figure is growing each year." The group predicts that by 2050 "humans will consume between 180% and 220% of Earth's biological capacity."

Running this enormous "overdraft" with the planet is going to have bad consequences, the group says. "Unless governments take urgent action, by 2030, human welfare, as measured by average life expectancy, educational level and world economic product will go into decline." The *Observer*, a British newspaper, summed it all up neatly in a headline: "Wanted: New Earth by 2050".

Are these extraordinarily pessimistic forecasts at all plausible? No, says an analysis by Denmark's Environmental Assessment Institute, headed by Bjorn Lomborg, author of "The Skeptical Environmentalist". Two main things are wrong with WWF's approach. First, the footprint is a difficult measure to make sense of.

Second, even if assorted environmental pressures could be aggregated in the way footprinters advocate, WWF's predictions would still look mysteriously gloomy.

In principle, there is nothing wrong with trying to come up with a common unit of environmental pressure, provided the simplification is useful rather than misleading. The footprint idea combines the area required for cropland, grazing land, forest products, fishing grounds, sustainable use of energy, and built-up land (making adjustments for the productivity of different sorts of space). In 1999, according to WWF, the total came to 13.7 billion hectares. But the group says that only about a quarter of the planet's surface, 11.4 billion hectares, is available to supply these services—hence the overdraft.

No room, no room

Why is this misleading? To begin with, the institute points out, the approach builds in questionable assumptions. Crucial is an implicit, and very strict, idea of sustainability, which in effect denies that natural resources can often be replaced or augmented by man-made ones.

This aside, the main drawback of the analysis is the way it treats energy. WWF defines the footprint for fossil fuels as the area of forest required to absorb emissions of CO₂ (excluding those absorbed by the oceans). Growth in the energy footprint then drives almost everything else. The energy footprint increased from 2.5 billion hectares in 1961 to 6.7 billion in 1999, the fastest-growing component of the overall footprint—and, by the end of the period, very much the biggest.

Exclude energy from the total foot-

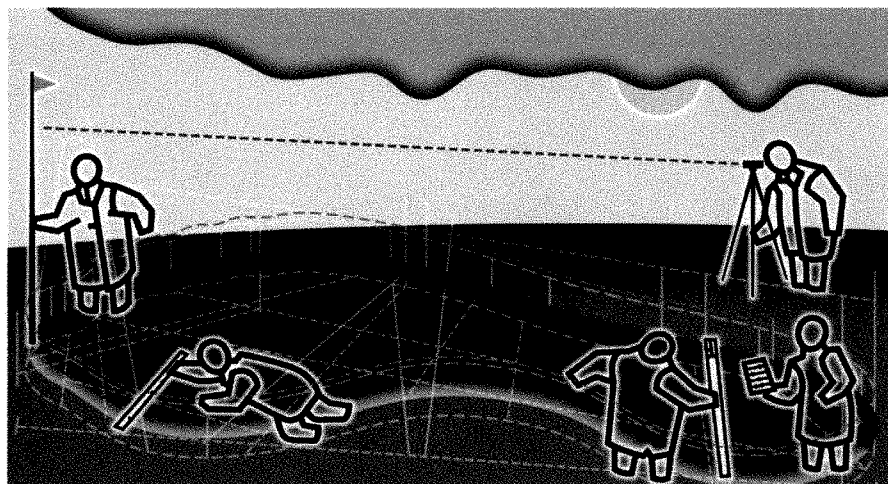
print, and it is harder to get alarmed. Growth in the ecological footprint excluding energy was much smaller than growth in global population between 1960 and 2000: that is, the ecological footprint per person, excluding energy, has been shrinking rapidly. Hardly a sign of reckless unsustainability.

So a lot turns on whether it is right to include the energy footprint in the aggregate measure—and on whether it is right to estimate this as the forest area required to absorb CO₂. On the first question, it is not obvious why sustainable development should require no change whatever in CO₂ concentrations, as the energy footprint implicitly demands. And even if sustainability did require this, there would be other ways of doing it—such as by increasing the use of renewable sources. Some renewable sources (such as windmills in deserts) make no demands on biologically productive space, which incidentally implies that the limit of 11.4 billion hectares for the area available to provide environmental services is wrong.

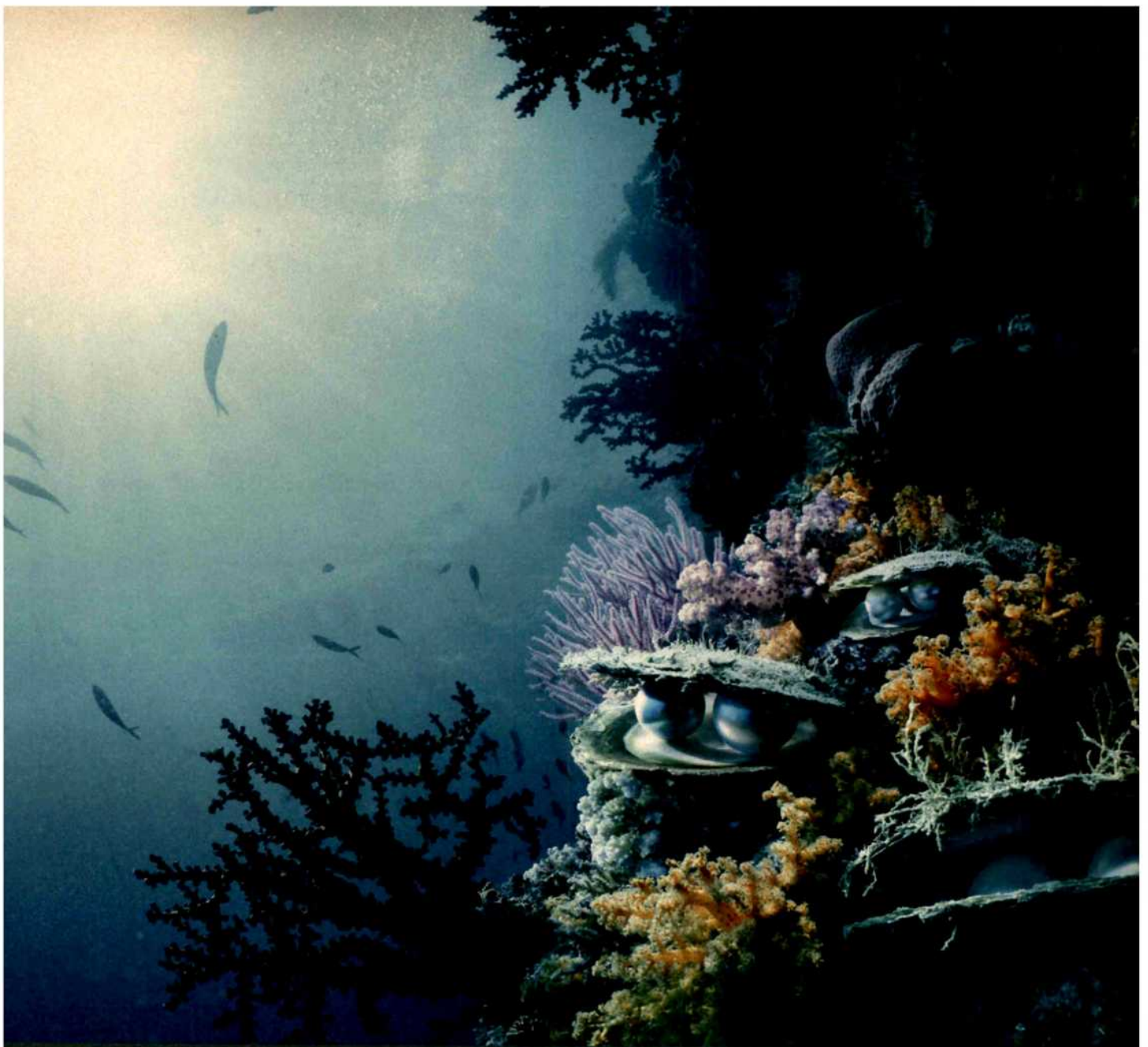
Framing the right policy on energy and CO₂ is complicated, to be sure. The point is, the footprint approach muddles the issue rather than simplifying it, apparently for the sake of yielding an alarming overall ecological deficit.

However, supposing everything WWF says about footprints is correct, how does the group come up with the catastrophe they have pencilled in for 2030? Between then and 2060 their projections appear to show average life expectancy across the world falling to less than 25 years. (The United Nations population division predicts that life expectancy will rise to nearly 80 years by 2060.) *Living Planet Report 2002* does not say how this cataclysm comes about. The underlying analysis has not yet been published, and Mr Lomborg's institute is at a loss. The answer cannot be global warming. By 2030, according to the Intergovernmental Panel on Climate Change, global warming will have added at worst one degree to global temperatures. How could this cause the global catastrophe WWF says it fears?

WWF is using an updated version of the model which the Club of Rome used in the 1970s to predict, among other things, that the world would run out of oil by 1992. Maybe that explains it. ■



Living Planet Report 2002 is available on WWF's website, www.panda.org. The Environmental Assessment Institute's paper can be found at www.imv.dk



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The Antikythera mechanism

The clockwork computer

An ancient piece of clockwork shows the deep roots of modern technology

WHEN a Greek sponge diver called Elias Stadiatos discovered the wreck of a cargo ship off the tiny island of Antikythera in 1900, it was the statues lying on the seabed that made the greatest impression on him. He returned to the surface, removed his helmet, and gabbled that he had found a heap of dead, naked women. The ship's cargo of luxury goods also included jewellery, pottery, fine furniture, wine and bronzes dating back to the first century BC. But the most important finds proved to be a few green, corroded lumps—the last remnants of an elaborate mechanical device.

The Antikythera mechanism, as it is now known, was originally housed in a wooden box about the size of a shoebox, with dials on the outside and a complex assembly of bronze gear wheels within. X-ray photographs of the fragments, in which around 30 separate gears can be distinguished, led the late Derek Price, a science historian at Yale University, to conclude that the device was an astronomical computer capable of predicting the positions of the sun and moon in the zodiac on any given date. A new analysis, though, suggests that the device was cleverer than Price thought, and reinforces the evidence for his theory of an ancient Greek tradition

of complex mechanical technology.

Michael Wright, the curator of mechanical engineering at the Science Museum in London, has based his new analysis on detailed x-rays of the mechanism using a technique called linear tomography. This involves moving an x-ray source, the film and the object being investigated relative to one another, so that only features in a particular plane come into focus. Analysis of the resulting images, carried out in conjunction with Allan Bromley, a computer scientist at Sydney University, found the exact position of each gear, and suggested that Price was wrong in several respects.

In some cases, says Mr Wright, Price seems to have "massaged" the number of teeth on particular gears (most of which are, admittedly, incomplete) in order to arrive at significant astronomical ratios. Price's account also, he says, displays internal contradictions, selective use of evidence and unwarranted speculation. In particular, it postulates an elaborate reversal mechanism to get some gears to turn in the right direction.

Since so little of the mechanism survives, some guesswork is unavoidable. But Mr Wright noticed a fixed boss at the centre of the mechanism's main wheel. To his instrument-maker's eye, this was sugges-

tive of a fixed central gear around which other moving gears could rotate. This does away with the need for Price's reversal mechanism and leads to the idea that the device was specifically designed to model a particular form of "epicyclic" motion.

The Greeks believed in an earth-centric universe and accounted for celestial bodies' motions using elaborate models based on epicycles, in which each body describes a circle (the epicycle) around a point that itself moves in a circle around the earth. Mr Wright found evidence that the Antikythera mechanism would have been able to reproduce the motions of the sun and moon accurately, using an epicyclic model devised by Hipparchus, and of the planets Mercury and Venus, using an epicyclic model derived by Apollonius of Perga. (These models, which predate the mechanism, were subsequently incorporated into the work of Claudius Ptolemy in the second century AD.)

A device that just modelled the motions of the sun, moon, Mercury and Venus does not make much sense. But if an upper layer of mechanism had been built, and lost, these extra gears could have modelled the motions of the three other planets known at the time—Mars, Jupiter and Saturn. In other words, the device may have been able to predict the positions of the known celestial bodies for any given date with a respectable degree of accuracy, using bronze pointers on a circular dial with the constellations of the zodiac running round its edge.

Mr Wright devised a putative model in which the mechanisms for each celestial body stack up like layers in a sandwich, and started building it in his workshop. ►►

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► The completed reconstruction, details of which appeared in an article in the *Horological Journal* in May, went on display this week at Technopolis, a museum in Athens. By winding a knob on the side, celestial bodies can be made to advance and retreat so that their positions on any chosen date can be determined. Mr Wright says his device could have been built using ancient tools because the ancient Greeks had saws whose teeth were cut using v-shaped files—a task that is similar to the cutting of teeth on a gear wheel. He has even made several examples by hand.

How closely this reconstruction matches up to the original will never be known. The purpose of two dials on the back of the device is still unclear, although one may indicate the year. Nor is the device's purpose obvious: it may have been an astrological computer, used to speed up the casting of horoscopes, though it might just as easily have been a luxury plaything. But Mr Wright is convinced that his epiclytic interpretation is correct, and that the original device modelled the entire known solar system.

The Greeks had a word for it

That tallies with ancient sources that refer to such devices. Cicero, writing in the first century BC, mentions an instrument "recently constructed by our friend Poseidonius, which at each revolution reproduces the same motions of the sun, the moon and the five planets." Archimedes is also said to have made a small planetarium, and two such devices were said to have been rescued from Syracuse when it fell in 212BC. This reconstruction suggests such references can now be taken literally.

It also provides strong support for Price's theory. He believed that the mechanism was strongly suggestive of an ancient Greek tradition of complex mechanical technology which, transmitted via the Arab world, formed the basis of European clockmaking techniques. This fits with another, smaller device that was acquired in 1983 by the Science Museum, which models the motions of the sun and moon. Dating from the sixth century AD, it provides a previously missing link between the Antikythera mechanism and later Islamic calendar computers, such as the 13th century example at the Museum of the History of Science in Oxford. That device, in turn, uses techniques described in a manuscript written by al-Biruni, an Arab astronomer, around 1000AD.

The origins of much modern technology, from railway engines to robots, can be traced back to the elaborate mechanical toys, or automata, that flourished in the 18th century. Those toys, in turn, grew out of the craft of clockmaking. And that craft, like so many other aspects of the modern world, seems to have roots that can be traced right back to ancient Greece. ■

GM crops in Africa

Better dead than GM-fed?

Europe's greens are helping to keep Africans hungry

SOUTHERN AFRICA'S food crisis is set to be the worst in a decade. Around 14.5m people are dangerously hungry, and many have been reduced to eating wild leaves and pig food. One might, then, expect food aid to be welcomed. But Zambia is refusing to accept American donations because much of its corn and soya is genetically modified (GM). Zambia's president, Levy Mwanawasa, calls the stuff "poison" and refuses to import it, despite a warning from the UN World Food Programme, on September 16th, that relief supplies in his country could run out in two weeks.

Africans have two reasons for being wary of GM food aid: one silly, one slightly less so. The silly reason is the suggestion that GM foods are a danger to human health. Americans have been chomping GM maize and soyabeans for seven years, without detectable harm. And compared with the clear and immediate danger posed by malnutrition, the possibility of being poisoned by Frankencorn seems rather remote.

The more sensible reason for being wary of GM foods is that there are people who, not being in any danger of starvation, are precious about what they eat. They are called Europeans. And their tastes matter enormously in Africa because countries such as Zambia earn much

of their hard currency from agricultural exports to rich countries, so any plausible threat to this trade has to be taken extremely seriously.

GM food aid is such a threat because if a Zambian peasant were to plant GM seeds from an aid shipment, these might pollinate (or, as Greenpeace puts it, "contaminate") neighbouring fields. Before long, farmers might no longer be able to convince European buyers that their products were GM-free—making them harder to sell.

While imports of GM food are not barred from Europe by law, consumers are so suspicious of them that supermarkets have constructed elaborate systems to certify that the food they sell is unmodified. Tesco, for example, a British supermarket, promises that there are no GM products in its own-brand food. It audits its suppliers to make sure they comply, and has samples of foods tested for traces of DNA that would indicate that some of the ingredients have been genetically modified.

The laboratory tests for GM ingredients do not work by screening for genetic modification *per se*, but look for already known pieces of DNA or protein that reveal the presence of recognised GM foods. In other words, the tests look for GM foods that have been registered and approved by at least one country's food-safety authorities. New and unknown GM ingredients wouldn't show up, says Neil Griffiths, head of Law Laboratories in Birmingham, England, a firm involved in the testing business. Testing is also difficult in highly processed foods. Oil derived from GM soyabeans, for example, cannot be tested as it often contains no DNA or protein.

While the testing regime is flawed, it is stringent enough to present a serious problem for farmers in poor countries who want to export their crops. The fears of pampered northerners are thus creating an obstacle to the acceptance of food aid and the adoption of technology that might make the poor less poor.

Other hungry countries in the region, such as Zimbabwe and Mozambique, have decided, despite initial reluctance, to accept GM food aid. In Zimbabwe, the government decided to tackle the problem of "contamination" by milling aid corn before distributing it, so that it cannot be replanted. (There are, though, concerns that seeds could still be stolen before the government is able to mill them.) Zambia may yet follow its neighbours' example; local scientists have been sent to Europe, America and South Africa to study the pros and cons of GM, and will report back shortly.

Europe's anti-GM hysteria, however, will continue to deter farmers in poor countries (the majority of the population) from planting crops which tend to have higher yields and require fewer applications of costly and dangerous chemical pesticides. Hardly a green outcome. ■



Food before fine words

Satellite launchers

The new jet set

Researchers are vying to build a system that will launch small satellites cheaply

IN SPACE, small is not yet beautiful. Even as engineers manage ever more miraculous feats of miniaturisation on the ground, the route to the skies remains dominated by massive rocket launchers spawned by manned space programmes. Satellite small fry (those weighing less than 100kg) can, if they are lucky, piggy-back on such launches. But that may mean waiting years to hitch a ride into space.

The lack of a cheap and flexible means of launching small satellites has been a problem for a long time. Now, military necessity may lead to a solution. America's armed forces want to launch small tactical satellites, such as spy satellites, on demand—for example, in response to the outbreak of a regional conflict. So, teams from six American firms are competing to design a jet aircraft that would fly to the edge of space and then launch a small satellite into an orbit low enough for spying, using an expendable two-stage rocket.

The project, known as RASCAL (Responsive Access, Small Cargo and Affordable Launch), is sponsored by America's Defence Advanced Research Projects Agency. The agency wants a vehicle that will put satellites weighing less than 75kg into orbit for about \$10,000 per kilo. Although this is no cheaper per kilo than launching large satellites, it is less than a fifth of the cost of using existing launchers specifically to put up small payloads. Moreover, employing a jet aircraft as a reusable initial stage for launching a satellite has another advantage—an aircraft could take off discreetly from any military airfield, and then make a secret satellite launch from anywhere within range.

The idea is that the jet would fly subsonically to an altitude of about 15km. It would then begin a supersonic-boost manoeuvre, shooting the aircraft on a ballistic trajectory out of the atmosphere. Once beyond the air, the craft would coast with its engines switched off. At the peak of its trajectory the doors of its satellite bay would open and the payload would be released, to be carried the rest of the way into orbit by a rocket. The aircraft would then fall back towards the earth, restarting its motors when the air was thick enough to support combustion, and fly home.

One of the key pieces of technology needed for the aircraft is a special booster for its engines. This is called a Mass Injected Pre-Compressor Cooled (MIPCC) system, and it works by injecting a fine

Out-of-body experiences

Transcendental medicine

Out-of-body experiences come from stimulating one part of the brain

AMERICAN football is often described as a game of inches. Neuroscience is much the same. Forward progress is difficult, and each stride small. And though the basic anatomy of the brain is known, it is not always clear what role each little part plays. Now neuroscientists think they may have pinned down the source of out-of-body experiences, phenomena that have long confounded scientists and delighted occultists.

While probing the brain of a woman who suffered from epilepsy, Olaf Blanke and his colleagues at the University Hospital of Geneva found that stimulating the right angular gyrus (a point about an inch above and slightly behind the right ear, and just inside the skull) caused her to feel that she was travelling out of her own body. In a treatment undertaken after more than ten years of drug therapy had failed, around 100 electrodes were implanted in the woman's brain. Over the course of a week, the electrodes were monitored to find the source of electric currents in the brain responsible for the seizures. For around 90 minutes each day, the electrodes were also stimulated to map the structure of the brain so as to identify language centres and other vulnerable areas.

When the current was first applied to the right angular gyrus, the woman reported that she was sinking into the bed, as if falling from a height. As he reports in *Nature* this week, Dr Blanke then systematically applied additional electric currents to the woman's right angular gyrus. When she looked at her legs during the stimulation, she saw them grow



shorter. Similarly, her left arm felt as if it was shrinking. But when her eyes were averted, the stimulation led to her apparently seeing herself lying in bed, from about two metres above it.

Though he stresses that the mechanisms involved are not fully understood, Dr Blanke supposes that such an out-of-body experience is caused when inputs from the "body schema"—the system that gives one a sense of one's own body—get out of synch with those from the vestibular system, which is responsible for balance. By deliberately disrupting this synchronisation, Dr Blanke can induce such experiences. This serendipitous discovery accompanies another pleasing result for the team in Geneva: after the removal of a small section of her brain identified by the study, the epilepsy patient is now back at work, almost fully cured of her seizures.

mist of water into the air ahead of the engines. That does two things. It cools the engines' compressors, stopping them from overheating as the plane goes faster. And it makes the air denser, which increases the thrust of the engines. This should allow the jet to travel farther and faster in the thin atmosphere of high altitude than would be possible for an aircraft powered by unassisted jet engines. Even that, however, will not be enough to take the craft out of the atmosphere altogether. At an altitude of 30km the MIPCC system must inject liquid oxygen into the engines to maintain thrust.

This is not the first time that rockets will be launched from jet aircraft. Many decades ago the American air force tested a similar idea as part of a programme to develop anti-satellite technology, but nothing

came of it. And Orbital Sciences, a commercial satellite-launching firm based in Dulles, Virginia, has been launching Pegasus rockets from a modified B-52 bomber for over a decade. But Pegasus is a three-stage device designed for much larger satellites than RASCAL's jet will carry. More significantly, RASCAL's craft will be unique because it will leave the atmosphere.

In December, the six competing teams will be narrowed down to one, or possibly two. The winner, or winners, will be awarded \$10m to refine their designs and test hardware. By 2006, a demonstration vehicle costing \$88m is planned. If a suitable design can be found, it might, besides offering military advantages, lead to the development of a low-cost way to launch small commercial satellites. Then anyone could have an eye in the sky. ■

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Eric Hobsbawm

Giving account

You can be wrong in politics without being a fool or a scoundrel

THIS autobiography, says Eric Hobsbawm, does not take the form of a post-mortem in which the corpse pretends to be the coroner. Fortunately for his readers, he is wrong. Inquest is in fact the best succinct description of "Interesting Times", a ruthlessly honest self-investigative book in which this eminent Marxist historian, born in the year of the October revolution of 1917, tries his best to understand and to explain why he is "a lifelong communist".

The gentle mockery in the "lifelong" label is deliberate. Mr Hobsbawm knows that the communism that inspired his generation at Cambridge in the 1930s, "the reddest and most radical generation in the history of the university", has predeceased him. "We thought we knew what the new world would be like after the old world had come to an end. In this, like all generations, we were mistaken."

No apologies, he thinks, are called for, and none is made. It was as a schoolboy in Berlin when Hitler came to power that the young Hobsbawm first became attracted to communism and he still believes it was the right response at that time and in that place. Nazi Germany was a monstrous evil and only Communist Russia could destroy it. Virtual history is all very well but, even now, "if you ask me to entertain the proposition that the defeat of National Socialism was not worth the 50m dead and the uncounted horrors of the second world war, I

Interesting Times: A Twentieth-Century Life. By Eric Hobsbawm. Penguin/Allen Lane; 448 pages; £20. To be published in America by Pantheon in August 2003

simply could not." He nonetheless concedes here, as he conceded in "Age of Extremes" (1994), his history of what he called the short 20th century, that communism was not just distorted but perverted when, under and after Stalin, the state interests of the USSR prevailed over the world revolutionary interests of the Communist International.

The universalism of the communist ideal still moves him. His father was an English Jew and his mother an Austrian one. They married in Switzerland. He was born in Alexandria in Egypt, and went to school in Vienna and Berlin. As a child of *Mitteleuropa*, with his background in the multilingual and multiconfessional Habsburg empire, he detests the nationalism of blood and soil everywhere. The behaviour of Israel's Likud Party, whose founders, he writes, were inspired by Mussolini, often tests the vow he made to his mother never to be ashamed of his Jewishness.

As well as cosmopolitan comrades, the certainty of eventual victory and the aesthetic appeal of a perfect and comprehensive intellectual system, his years as a communist activist also provided him with the

experience of fraternity—an experience reinforced by his war-time service. Confined to menial roles by the suspicions the brass-hats held about his loyalties, he worked alongside the workers of hand, whom he came to admire as well as like. Perhaps in consequence, Mr Hobsbawm is not an intellectual or any other sort of snob.

With a wry grin he recalls speeches at Marxist conferences so boring they pushed delegates into the streets, and a Communist International journal which, "even by the exacting standards of the Soviet era, must have been the all-time champion of unreadability". Yet he remains such an intensely partisan animal that he will automatically support any football team playing a country, like Croatia, that had a nasty right-wing past. Characteristically, the political overwhelms the personal in his autobiography. He is, as he says, a historian, not a gossip-columnist, and has no interest in lifting the sheets. His ever-sociable wife, Marlene, makes a few cameo appearances, but his children and grandchildren hardly get a mention.

Sadly, you only glimpse his enthusiasms. In his mid-80s, Mr Hobsbawm remains curious about everything, from the poems of Kipling which he imbibed as a boy to the birdsong of blackbirds to the incomes of hill farmers of rural Wales, a place that he has come to love. The great recreational passion of his life is jazz and it takes up a sizeable chunk of "Interesting Times". Typically for him, it has a political dimension. It was through jazz that he threw himself into an early anti-racist campaign after race riots in Notting Hill in the late 1950s. As his party faith had seriously weakened when Russian tanks crushed the Hungarian uprising in 1956, he did not try hard to turn that pro-immigrant campaign into a communist front. ■

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18th-century science

Before there were departments

The Lunar Men: Five Friends Whose Curiosity Changed the World. By Jenny Uglow. Farrar, Straus and Giroux; 512 pages; \$30. Faber and Faber; £25

IN THE middle decades of the 18th century a group of clever, merry, Birmingham men gathered every month on the Monday night nearest to the full moon to discuss pretty much everything under the sun. There was Erasmus Darwin, an enormously fat doctor, Matthew Boulton, a pushy metal-goods manufacturer, and Josiah Wedgwood, the man who turned fine pottery into a commercial goldmine. They were joined on occasions by James Watt, the engineer who fine-tuned the steam engine, and Joseph Priestley, a burning radical who discovered oxygen.

As these brief resumés suggest, the members of the Lunar Society were men of huge and varied talents. In an age before intellectual specialisation, it was not uncommon for a factory owner to read philosophy or for a doctor to play the flute beautifully. However, at the heart of the Lunar men's interests lay a driving curiosity in the workings of the natural world (fittingly, they had chosen the full moon to meet because it gave the most light as they stumbled home, drunk on fine ideas and clever talk). Together and separately, Darwin, Wedgwood and their friends classified fossils, made telescopes, created sparks of electricity, and came up with scores of ingenious suggestions for the world's improvement (this included tow-

ing icebergs from the Arctic to the equator to even out the climate).

Jenny Uglow has done that difficult thing of writing a group biography that gives equal attention to all the main players, yet still manages to be something more than a patchwork. With her sure grasp of the social and political passions driving the times, she is able to situate her clutch of subjects in a very particular intellectual tradition. Most of the Lunar men were from non-conformist backgrounds and so not part of an Oxbridge-educated elite. Either they went to Scotland to be taught, or else they learned at their father's workbench, picking up practical scraps that, combined with evening study, cohered into a system of proper knowledge. All of them, as might be expected, were restless, questioning, convinced that there were new and better ways of doing things—whether that involved writing a poem on the sex lives of plants or building a canal. With pardonable exaggeration, Ms Uglow in her introduction credits the Lunar men with nothing less than inventing the modern world.

Scientific experimentation in these times was a risky business, full of sudden bangs, sour smells and unexpected textures, and the author is marvelously good at capturing this sensuous world, far removed from white coat sterility. Where she also scores highly is in her deft way of linking this narrative of exploration and achievement with a more hidden, ambling story of love affairs, humdrum marriages, disappointing children and exhausted endings. The result is an absolute wonder of a book, huge in its span and close in its detail, nothing less than a snapshot of what and who was best about Britain and its intellectual life in the middle of the 18th century. ■

Human nature

Who's afraid of the new science?

The Blank Slate: The Modern Denial of Human Nature. By Steven Pinker. Viking Press; 528 pages; \$27.95. Penguin/Allen Lane; £25

AT A film your bliss is disturbed by the chatter of small children. What is it, you wonder, about dark rooms and bright screens that loosens little kids' tongues? Then their parents start rabbiting away over the popcorn, and the answer becomes obvious: they taught their spawn to act this way. But hold it, say behavioural geneticists. What if the children inherited a gabby disposition straight from the parents in their cocktail of genes? Learning could well have had nothing to do with it.

Steven Pinker's provocative new book is full of catchy examples like this that he uses to highlight two radically different ways of conceptualising and explaining our behaviour: one with an eye to culture, learning and the social sciences, the other with an eye to nature, genetic inheritance and experiment. He makes no bones about where he stands. Social science and its popularisers have, he thinks, systematically ignored or derided recent strides by neuroscience, artificial intelligence, behavioural genetics and evolutionary psychology. Though he seems to have a point to score or a joke to crack about almost every topic on earth, he makes his main argument persuasively and with great verve.

This is territory where dust soon flies and tempers are quickly lost: remember Richard Dawkins and Stephen Jay Gould? Luckily, Mr Pinker rarely loses his cool. "The Blank Slate" ought to be read by anybody who feels they have had enough of nature-nurture rows or who thinks they already know where they stand on the science wars. It could change their minds.

If nothing else, Mr Pinker's book is a wonderfully readable taster of new research, much of it ingenious, designed to show that many more of our emotional biases and mental aptitudes than previously thought are hard-wired or, to use the old word, innate. Further, because humans are genetically speaking a fairly homogeneous species, people the world over are more alike in deep ways that matter than may appear from superficial differences of culture. The book ends with a startling list of more than 300 so-called human universals published originally by Donald Brown in 1991 including not only the presence everywhere of childbirth rites, incest taboos and beliefs about death—we expect that—but, more surprisingly, the existence in all societies of, for example, repertoires of facial expression for a few basic emo- ➤



The sublimities of science

► tions that do not themselves vary from culture to culture.

Confusingly, Mr Pinker gives two reasons why people resist this new science, one more convincing than the other. His weaker explanation is the alleged appeal of three myths: the blank slate, the noble savage and the ghost in the machine. Nobody could consistently hold all three at once, and only the blank slate—an idea famously expressed by John Locke in the 17th century when he called a newborn's mind "white paper devoid of all characters"—is really relevant. Mr Pinker brings in the noble savage—belief in the gentleness of primitive man—and the ghost in the machine—reluctance to abandon an immaterial mind or soul—largely for the polemical fun of torching a few straw men.

The idea of a blank slate came to underpin 20th-century behaviourism, typified by B.F. Skinner, for whom human beings were little more than conditioned automata. It was a working hypothesis of sociology and anthropology that looked for the basis of our beliefs and attitudes in teaching and social practice, not in the contents of the fledgling brain. Blank-slatism reached its nadir, in Mr Pinker's view, in the post-modernist claim that all human attitudes and categories of thought—even gender—are a social construction.

Beyond the two camps

At this point, it would have been neater for a two-camps approach if hard science, as Mr Pinker calls it, were united against the rogues and cretins of cultural relativism in rejecting the blank slate. But, ever honest, he admits that the blank slate still has defenders among tough-minded and experimental researchers: in artificial intelligence, "connectionists" who think brains work like neural networks simulated on computers "learning" from statistical patterns with only weak constraints on their inner structure (the near-blank slate); and in neuroscience, defenders of neural plasticity: the view roughly that the brain is a flexible and general-purpose learning device rather than a pre-packed box of specialised tools determined by our genes (the rewritable slate). If truth be told, blank-slate empiricism is still the basis in many experimental psychology departments where the innatism Mr Pinker champions is treated as a dodgy bet.

So if the noble savage and the ghost in the machine are irrelevant, and if even "hard" science disagrees about the blank slate, what is hostility to the new research due to? Fear—Mr Pinker's second answer—is altogether more convincing.

One fear is of inequality. If science shows that our inborn endowments are unequal, will that not legitimise unequal treatment? Another fear is of imperfection. If science shows we are less changeable than hoped, will schools and social

New fiction

We'll think of something

A Whistling Woman. By A. S. Byatt. *Chatto & Windus*; 436 pages; £16.99. To be published in America by Knopf in December

"THIS isn't the end," expostulates Leo, Frederica's small son, as the serial story being read to him comes to a final stop. You feel the same about "A Whistling Woman", the last in A.S. Byatt's magnificent quartet of novels on intellectual life and thought in the 1950s and 1960s. But 1970 has been reached, a scattering of the characters on her huge canvas have been killed off, or paired off, and it is time to stop.

"A Whistling Woman" can be read on its own. Rich in metaphor and glancing allusion, it is a tale of learning and anti-learning, sects and cults, the complex sexual relationships of humans and snails. The snails, the pursuit of two scientists, get locked away behind the fence of a self-destructive community led by a charismatic blood-haunted Manichee. The minor humans, a fairground of oddities, are named with Dickensian ear: Elvet Gander, a creepy psychoanalyst, Avram Snitkin, an itinerant ethnomethodologist, Mickey Impey, a pretty pop poet, Jonty Surtees, an agitator, Eva Wijnobel, a terrible astrologer.

A knowledge of the earlier books does, however, help. Some characters must seem two-dimensional without knowing, beyond a brief recap, what has made them as they are: guilt-ridden, for instance, or melancholic. Frederica, for one, will suffer from reading the new book only. Born (like her author) in 1936, her life threads through all four volumes. Clever, thin, pushy Frederica reaches for the sky, and keeps falling. A natural academic, possibly creative (though her only book sounds a ghastly 1960s con-



traption), she ends up a mini-celebrity on a TV chat-show, feeling, in her words, "a mermaid in a raree-show".

But "A Whistling Woman", like its predecessors, is predominantly a novel of ideas. Not about politics, foreign or domestic, but about philosophy, psychology and literature; the excitement of genetics and computer science edging towards their breakthrough. As before, Ms Byatt has to find a framework for all this thought: a book embedded in a book, a university seminar on body and mind, television discussion. As before, some of the talk invites a bit of skipping. But then the narrative resumes, pulling you along. It makes a fine conclusion to the quartet, leaving you properly thoughtful. "We haven't the slightest idea what to do," says Frederica at the end. "We shall think of something," says her lover.

improvement be pointless? If parental example, as opposed to genes and luck, has little effect on how children turn out, will that encourage indifference and neglect? No, Mr Pinker says, these fears confuse findings of fact with social aims and human values. In sum, he is saying, the new science of man will probably leave most of our moral and political arguments at the starting gate. Not everyone will be so sanguine. But Mr Pinker's approach does show how little of the new research can be squeezed into left-right or liberal-conservative boxes. This is a breath of air for a topic that has been politicised for too long.

Two final points in favour of "The Blank

Slate" are these. Unlike many new-science popularisers, the book never underplays the mind's complexity. Nor does it revel in juvenile smugness about the human condition. In one of his best chapters, "The Many Roots of Our Suffering", Mr Pinker suggests that conflict between the drives which evolution has landed us with and the aptitudes that would now help us prosper is probably inevitable. Scientific knowledge can at least aid us in managing this conflict, and denying science will almost certainly make it worse. In the words of Anton Chekhov, one of Mr Pinker's favourites, "Man will become better when you show him what he is like." ■

Festival films

Petersburg magic and Rio gangs

TELLURIDE, COLORADO

A couple of gems from the festival of independent film at Telluride

CINEMA today is all too often just about plot or special effects. So films that are true to the medium, successfully weaving together sound, image and time to tell a really cinematic story are always special. On show at Telluride earlier this month were two remarkable examples.

Alexander Sokurov's "Russian Ark", which opens in the United States in November, explores the 300-year-long history of the Hermitage museum in a single "breath", an uncut 90-minute walk through 35 of its rooms and halls. This has never been done before, and the result is, among other things, a magical rumination on what film can achieve.

Tilman Büttner, the director of photography who operated the steadicam used to shoot the film, has turned the camera into one of its main characters, a contemporary film maker trapped in a journey through Russian history, with Mr Sokurov himself speaking its part. As we move from room to room an array of different scenes come up—Peter the Great whipping one of his generals, for example, or present-day visitors enjoying the works of art. The camera is invisible to the film's other characters, apart from a fellow time-traveller, a 19th-century French diplomat. The relationship between the camera and the diplomat, against the backdrop of some of Europe's greatest works of art, reveals the main theme of the film, Russia's uneasy link to its past and to Europe.

In contrast to the expanse of the subject, the film was shot in a single day, using almost 1,000 stage actors, hundreds of extras, two orchestras and 22 assistant directors. Cast and crew had not rehearsed together until production day. Yet they have turned out a seamless film. If the camera were to shake, Mr Büttner would lose his tight containment of the scene and the audience would remember the film maker's conceit. The dynamic between Mr Sokurov's lyrical movement through historical time and Mr Büttner's real-time movement of the camera creates the tension needed to sustain the long shot.

If Mr Sokurov chooses a single technique to tell a complex tale, then just as interesting is Fernando Meirelles's multi-tiered "City of God", a film about gang violence during the 1960s and 1970s in Rio de Janeiro's *favela* of the same name. "City of God", which will be released in January, is a fine example of Latin America's recent film renaissance. It was shot on location,

using only natural lighting. The actors were mainly non-professional children from the *favelas*; the script was only there to suggest and guide the dialogue.

This naturalistic approach has echoes in the film's structure and tonal palette. Mr Meirelles divides the film into three parts. In the first, life is simple and crime relatively innocent. The compositions are ordinary, the angles conventional. The actors are given strict marks—literally, tape on the ground marking their positions—and the cinematography is warm. In part two, violence is on the rise, yet there is still a sense of freedom and possibility. Mr Meirelles uses more hand-held cameras as well as narrow lenses and bright Technico-

lor film to create a sense of excitement. The actors are given fewer marks and more freedom to improvise their lines. In the final third, chaos reigns and hope is dead. Mr Meirelles wanted to create the effect of losing control. The tone is monochromatic, the camera swings wildly and the actors have no marks at all.

Far from being a distraction, these aesthetic characteristics confirm just how good Mr Meirelles is at creating energy on screen. From the opening scene, cutting quickly between black screen, a knife being sharpened and people dancing, before the camera chases off after a chicken in the alleys of the *favela*, we know that we are in the hands of a serious creative talent. ■

Film openings

Girl crazy

LOS ANGELES

No doubt about it, these girls will drive you nuts

STRANGE girls, whether genuine oddballs or digital holograms, are the theme of two new American films.

The Pygmalion myth gets a brainy workout in "Simone", written and directed by Andrew Niccol, who scripted "The Truman Show", a media satire about a real person in a fabricated world. Here it is the reverse. Simone (say it "Simone") is a synthesp, a digital film star whose fractured monicker is short for "Simulation One". She is the creation of a film director, Viktor (as in Frankenstein) Taransky, who has become fed up with the egomania of the authentic article. As Taransky is played by Al Pacino, the film's subtext is the confrontation between this flesh-and-blood wizard of method acting and his virtual Trilby, whom Rachel Roberts plays two-dimensionally—that is to say utterly believably.

But trading in the real thing for a pliable fabrication doesn't solve his problems. When Simone's cool beauty and mysterious aloofness drive audiences wild, she quickly eclipses her unhappy creator. To his horror he finds that he cannot turn her off, even though every word and gesture is his, mimicked and transposed by computer. Film historians can fill in real-life parallels, from Josef von Sternberg and Marlene Dietrich down to Alfred Hitchcock and Tippi Hedren. In truth, there is very little in "Simone" that couldn't happen because most of it already has.

There is more girl trouble, though real this time, from Lee Holloway, the heroine of "Secretary", an independent film from a debut director, Steven Shainberg, that won the top prize at the Sundance film festival last February. It gives a new twist to the screwball comedy, she being



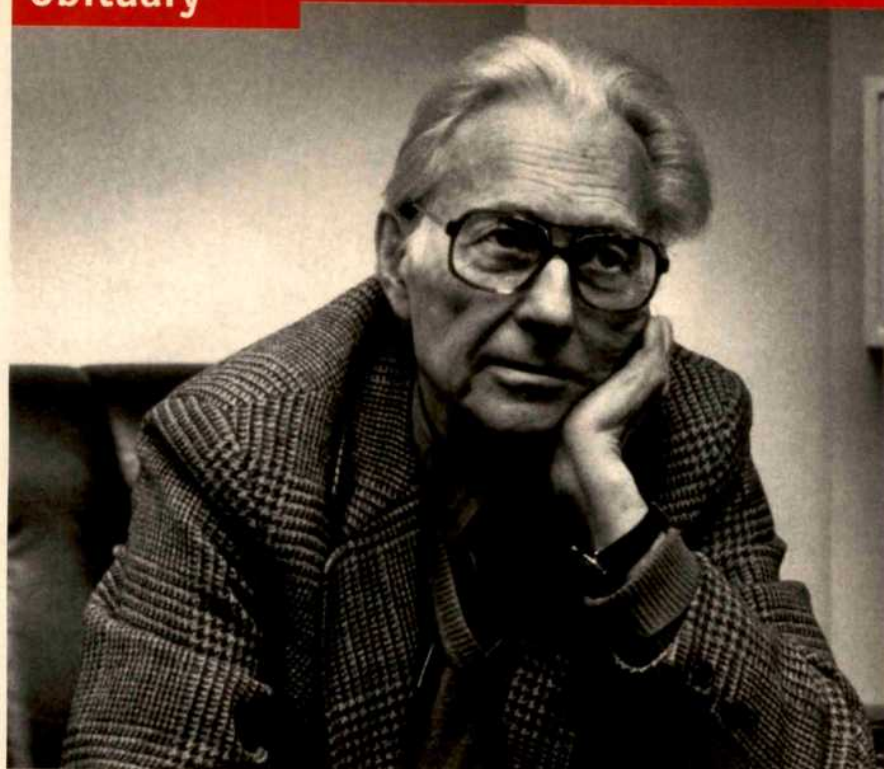
You wicked synthesp, you

a masochist, he a sadist.

Lee, played by Maggie Gyllenhaal, answers a help-wanted ad placed by E. Edward Grey (James Spader), a lawyer who wants a bit more from his secretary than typing and answering the telephone. Lee, a suicide survivor who has kinks of her own, senses a kindred spirit when she sees Mr Grey's advertisement and energetically pursues correction by committing intentional typing errors.

The film has a fairytale glow because that is how the world looks to Lee once Mr Grey is there to dictate and impose. It's too bad this visual key is later forgotten when Mr Grey flees commitment, one improbability follows another and the film seems to be going to pieces.

Mr Spader nevertheless puts in a deft turn as Lee's reluctant Gilles de Rais, and "Secretary" is also blessed with an authentic screwball in Ms Gyllenhaal. Her remarkably expressive face morphs from Rossetti to middle Picasso and back whenever some new off-kilter thought enters Lee's mind. If Hollywood can find the right roles for her and cuteness fatigue doesn't set in, hers will certainly be a career to watch.



William Phillips

William Phillips, a radical editor, died on September 13th, aged 94

FOR more than 40 years William Phillips edited *Partisan Review*, a magazine of small circulation and little money but with a great deal of influence. Writers and commentators whose words later commanded audiences of millions first saw their names in print in a publication that might sell 15,000 copies if things were going well. Mary McCarthy, Bernard Malamud and Saul Bellow were apprentice contributors. European stars such as Jean-Paul Sartre and Albert Camus were introduced to American readers through the *Review*. The magazine was defending T.S. Eliot, Franz Kafka and James Joyce long before their acceptance as central to modern culture.

Magazines of modest means are being born continually wherever there is a computer, or even a typewriter: Canada, not the world's greatest literary centre, has nonetheless given birth to at least 18 poetry magazines in recent years. Mr Phillips, who called himself a "cocky kid driven by a grandiose idea", provided evidence that a little magazine can even succeed. He could have joined what are sometimes called the "fat gods" of publishing. His skills of editing and spotting talent were very marketable. He must have been tempted to rescue himself from the slavery of a small business and join a publication where the pay was never late, where there

were holidays and secretaries did the office chores.

Some innovative magazines started in a modest way have done well commercially, among them *Time* (started in 1923) and the *New Yorker* (1925). But the *Review* was started in 1934 partly as a rebellion against what Mr Phillips saw as slick, watered-down presentations of serious ideas in literature and politics. That kept him head-down at the *Review*, even if he had to answer the telephone himself, and he and his wife Edna had to do part-time teaching to pay the phone bill. If Mr Phillips and his partisans had anything in common with the *New Yorker* crowd, it was in their love of socialising.

Talk, talk, talk

The *New Yorkers* ate, drank and argued at the Algonquin Hotel; Mr Phillips preferred Stewart's Cafeteria in Greenwich Village, where you could get a good meal for 75 cents, a sound basis for hours of malicious gossip, or the conduct of love affairs, as well as for arguments about politics. In later life Mr Phillips said that he had "pissed my time away with talk", talk of "sense and nonsense, idealism and cynicism". Perhaps he did: he often complained of the artistic malady known as writer's block. On the other hand, there

was the zest of "being in the midst of a community of so many talented, intelligent people". The talk produced the polemic bite, the topical excitement that made the *Review* worth reading.

Mr Phillips's father was a lawyer from Odessa. Like many Jews tired of tsarist persecution he pulled up roots and came to New York to join a community that has probably done most to provide America with its culture. His son dropped the family name of Litvinsky for the blander one of Phillips. He had some formal education, including a course in literature at New York University, but like many in his circle, he was mostly self-taught. In "The Oasis" a novel by Mary McCarthy, she describes Philip Rahv, who helped Mr Phillips to start the *Review* and was for many years his co-editor: "Facts of any kind, oddities, lore, local history...Bohemian women, downtown bars, argument, subways, news-stands, the office...this was [what] he knew of the world."

The *Review* was started with \$800 collected by sending a hat round at a political meeting. Some who chipped in their dollars believed that the magazine would take a communist line, favoured by many intellectuals at the time of the great Depression. But William Phillips and Philip Rahv were among the first on the left to acknowledge that liberty was being crushed in the Soviet Union, and the magazine attacked eminent commentators who, despite the evidence of those who had escaped from the Russian prison-state, were still "licking Stalin's boots". They opposed isolationism in America: a notable essay by George Orwell gave warning of German expansionism under Hitler.

While sharing political views, the two men often quarrelled over what should go into the magazine, which was published first as a monthly and later as a hungry quarterly. They had a "bickering marriage", said a friend. Rahv had fits of brilliance but had fits of depression too. William Phillips had the more balanced personality. What kept them together was their pampered child, the *Review*. The marriage lasted until 1969, when Rahv left to start his own magazine. He died in 1973.

It is difficult to say when Mr Phillips gave up editing. Perhaps he never did. In 1978, Edith Kurzweil, an academic, became joint editor of the *Review*. The couple were married in 1995 (Edna had died in 1985). Mr Phillips was 88 and still reading manuscripts. He said he remained a radical, but by then no one in America was much bothered about radicalism. The great debate between left and right had faded into gentle sparring between conservatives and liberals, and it was sometimes difficult to tell the difference. A melancholy William Phillips remarked in old age, "The future has not turned out so well." ■

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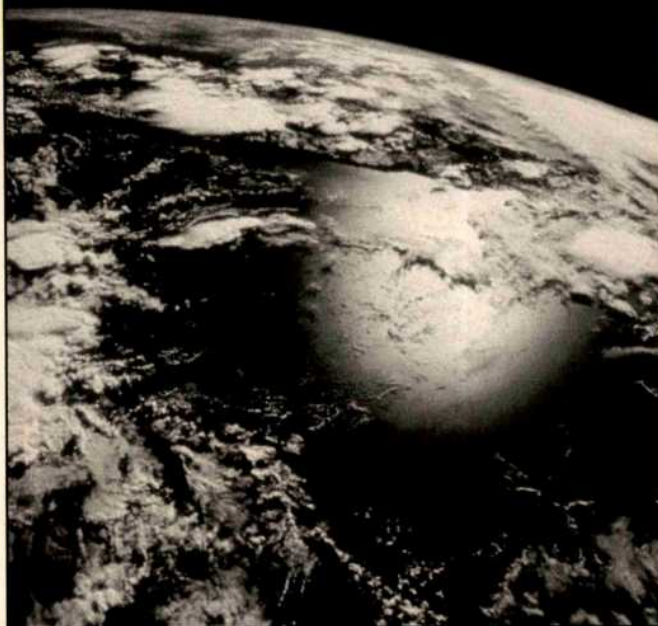
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Europe +44 20 75048280 cpEurope@careerpath.co.uk
Asia / M. East / Aus +66 2 2674688 cpasia@bkk.loxinfo.co.th



The Department of Economics at the National University of Singapore invites applications for faculty positions in all fields of Economics. Although it is likely that several positions will be filled at the entry level, applications from scholars with established records in research and teaching for available positions at the level of Associate Professor and Professor, are particularly encouraged. The department offers an attractive package of salary and benefits including subsidized housing and education, an environment conducive to scholarly research, and has an established reputation for good teaching at both the undergraduate and postgraduate levels. The medium of instruction, as well as the national language, is English.

Applications are invited for both regular and visiting positions, and should be submitted, together with a recent curriculum vitae, to:

**Professor Åke Blomqvist, Head, Department of Economics,
National University of Singapore, 1 Arts Link, Singapore 117 570**
[e-mail: ecshead@nus.edu.sg]

The deadline for application is December 31, or when the positions are filled. More information about the Department is available at www.fas.nus.edu.sg/ecs/

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• Advertising/PR/Consumer Behaviour • Services and/or Retail Sector Marketing • E-commerce	• Business English • Business Spanish • Human Resource Management/Organizational Behaviour

Responsibilities of the posts include:

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- supervising student projects and theses
- supporting the further growth and expansion of our department in strategic and daily operations

For further information, please contact Prof. Dr. Michael Lederer: lederer@fh-furtwangen.de or "http://www.fh-furtwangen.de".

Applications should be addressed to the Rector, University of Furtwangen, Postfach 1152, D-78113 Furtwangen, to arrive not later than October 18th, 2002.



NUFFIELD COLLEGE
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Official Fellowships in Sociology

The College proposes to appoint, with effect from 1st January 2003, or as soon thereafter as may be convenient, two Official Fellows in Sociology. Official Fellowships are comparable with tenured research Professorships; holders are expected to supervise doctoral students, but have no course or lecturing obligations. Nuffield College is a social science graduate institution, within Oxford University, with a strong research tradition of empirically informed and theoretically aware sociology. It is expected that the new appointments will strengthen that contribution to sociology. There is no restriction on substantive field.

Salary on a scale rising to £56,635 p.a. generous research allowance; details from the Warden's Secretary, Nuffield College, Oxford OX1 1NF, UK (e-mail: sociology.fellowship@nuffield.ox.ac.uk) or at www.nuff.ox.ac.uk Applications should be received by 30th September 2002.

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- supervising and reviewing the work of team members.

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For more information on UNESCO's programmes, consult our website:

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To apply, address a detailed curriculum vitae in English or French, indicating birth date, nationality and gender, attaching an identity photograph and copies of diplomas to: UNESCO, Chief, Recruitment and Staffing Section, Bureau of Human Resources Management, 7 place de Fontenay, 75352 Paris 07-SP, France, quoting post number IOS-902, before the deadline of 21 October 2002. N.B. Candidates may be considered for a similar P-4 post in IOS if an opening occurs in the near future.

Applications from qualified women candidates are encouraged, as are applications from under- or non-represented Member States.

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Research Fellow/Postdoctoral Fellow, MSSD (REF. #01-164)

IFPRI seeks a qualified candidate to serve as a Research Fellow/Postdoctoral Fellow for a three-year, fixed term, renewable appointment for its Markets and Structural Studies Division. This position is based at IFPRI headquarters located in Washington, DC but may involve travel to any of the countries in which IFPRI carries out its research.

The Research Fellow will conduct research on issues related to the role of institutions in the development and functioning of agricultural markets and management of infrastructure. The Fellow will work on the impact of institutions on transaction costs, and the micro-economic behavior of market actors in developing economies.

Required Qualifications: A Ph.D. in Economics, Agricultural Economics, or related field. Experience of empirical policy-relevant research on agricultural markets in developing countries; strong capabilities in quantitative analysis; ability to use economic theory in innovative and policy relevant ways; experience in collecting and analyzing primary survey data; ability to work in multi-disciplinary teams, ability to travel extensively; and strong communication skills in written and spoken English. Excellent knowledge of new institutional economics and econometric techniques related to market analysis required.

Preferred Qualifications: Work experience in East Africa or South Asia highly preferred. Other language skills desirable.

Postdoctoral Fellow/Research Fellow - MSSD and TMD (REF. #01-165)

IFPRI seeks a qualified economist to serve as a Postdoctoral Fellow or Research Fellow for an inter-divisional activity between its Markets and Structural Studies and Trade and Macroeconomics Divisions. This is a two-year, renewable appointment.

The Fellow will be responsible for estimation of Producer Support Estimates (PSE)/Consumer Support Estimates (CSE), and analysis of associated trade and other agricultural policies in several developing countries. Research is typically conducted in collaboration with researchers from developing countries. The Fellow is expected to travel and collaborate with country researchers.

Required Qualifications: Ph.D. in Agricultural Economics or related field; experience in developing country food and agricultural policy analysis; excellent quantitative Economics skills; fluency in English, including good writing and presentation skills; ability to work in multi-cultural settings; and ability and willingness to travel internationally.

Preferred Qualifications: Experience in computation of PSE/CSE, effective rates of protection, and policy analysis matrix; issues related to WTO's Agreement on Agriculture, skills in languages other than English; research and/or policy experience in developing countries.

IFPRI is an international organization and believes staff diversity contributes to excellence. We therefore encourage women and developing country nationals to apply. IFPRI offers a stimulating, collegial research environment with competitive salary and excellent benefits.

Applications: Submit resume, salary requirements, a detailed letter of interest summarizing the relevance of your experience, and the names of at least three references to: IFPRI Human Resource Services, REF. # 01-164 or REF. #01-165, 2033 K Street, NW, Washington, DC 20006, Fax: (202) 862-8187. E-mail: IFPRI-HRINTL@cgiar.org. When applying, please quote all job reference numbers in all queries and correspondence. For more information on IFPRI, its mission, and other job vacancies, please visit our website at www.ifpri.org. EOE.



Government of Democratic Socialist Republic of Sri Lanka
Sri Lanka Central Bank Strengthening Project

INTERNATIONAL LEGAL CONSULTANT FOR LAW REFORMS PROJECT IN THE FINANCIAL SECTOR

Credit No. 3525 CE

Expressions of Interest

This request for expressions of interest follows the general procurement notices for this project that appeared in UN Development Business on 16th October 2000 and 16th July 2002.

The Government of Democratic Socialist Republic of Sri Lanka (GOSL) has received a credit from the International Development Association (IDA) toward the cost of Sri Lanka Central Bank Strengthening Project, and intends to apply part of the proceeds of this credit to payments under the contract for the procurement of services of an international legal consultant for law reforms in the financial sector.

The Central Bank of Sri Lanka (CBSL) has embarked on a modernisation program which includes a comprehensive review of the financial sector legislative framework affecting the Central Bank, the banking sector and non-bank financial sector with a view to developing a modern and appropriate legislative infrastructure to support the development of a sound financial sector and its regulation.

Tasks

The international legal consultant will be assisted by a suitable local legal expert appointed by the CBSL. The international legal consultant is required to undertake a complete review of all financial sector legislation and other supporting legislation (including laws relating to electronic transactions) in the financial sector with a view to consolidating, rationalizing and recommending a general framework for the regulation and development of the financial sector including money and capital markets.

The international legal consultant is also expected to review the draft legislation that is already being prepared by the Central Bank incorporating the amendments which are urgently required as part of the financial sector reforms.

Qualifications

He/she must have recognized expertise of at least 10 years in central banking and banking law and proven expertise in advising either a central bank or the

regulatory authority of the banking sector in legal reforms reform projects. Good legislative drafting skills and practical knowledge of drafting central banking and banking directives and regulations are prerequisites. He/she must have substantial experience in advising a central bank in financial sector development issues and related legal matters. Cross-country experience in the relevant area is preferred.

Time Frame

The assignment will be for a two year period on a full-time basis. Initially the assignment would be for one year and will be extended for a further period of one year after a performance review of the work of the consultant.

Selection Method

A consultant will be selected in accordance with the procedures set out in the World Bank's guidelines: Selection and Employment of Consultants by World Bank Borrowers, January 1997 (Revised September 1997).

Invitation

The CBSL now invites eligible consultants to indicate their interest in providing the services. Interested consultants must provide information indicating that they are qualified to perform the services (description of similar assignments, experience in similar conditions).

Further details

Interested consultants may obtain further information at the address below from 0800 to 1615 hours from Monday to Friday.

Closing date

Expressions of interest should be delivered to the address below on or before October 21, 2002 before 10.00 a.m., under sealed cover.

Ms S Kadirugamawa

Director - Legal

Central Bank of Sri Lanka

No. 30, Janadhipathi Mawatha,

Colombo 1, Sri Lanka.

Telephone : 94-1-477550 Fax : 94-1-477745

E-mail : sarojini@cbsl.lk

Website : www.centralbank.lanka.org

"Promoting economic growth and higher living standards in developing countries"

Chemonics International, a leading consulting firm implementing activities to support international development in more than 100 countries, seeks senior consultants to help the transitional government in Afghanistan institutionalize sound economic policies. Experts are needed in the following sectors:

- **Fiscal Reform**
Macroeconomic policy, tax policy, tax administration, customs administration, budget planning, intergovernmental finance
- **Banking Reform**
Commercial banking, macroeconomic program, regulatory framework reform and enforcement, payment system, off-site supervision, accreditation process, training
- **Trade Policy**
Trade promotion strategy, legal reform, exchange rates, customs tariffs
- **Legal and Regulatory Reform**
Investment law, commercial law, competition policy, corporate governance, accounting reform, dispute resolution, legal training, public utilities
- **Privatization**
Central banks and public sector enterprises, legal framework, financial review, public awareness

You must have an advanced degree and at least 10 years of relevant professional experience including experience working in the developing world. Candidates with regional experience, and history of working on and/or managing large, complex development projects for USAID preferred.

Please send resume to jasmussen@chemonics.com by September 30, 2002. Only short-listed candidates will be contacted.

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The Woodrow Wilson School also offers a two-year Master's degree in Public Affairs (M.P.A.) and a Ph.D. degree program.

Princeton University and the World Bank invite applications for the Robert S. McNamara Fellowship Program, which provides full funding for qualified mid-career professionals from developing countries to attend Princeton's Master in Public Policy program. This rigorous program provides rising leaders in international and domestic public policy an opportunity to develop their economic and policy skills in an academic environment recognized the world over for excellence.

Financial Assistance: McNamara Fellows receive a full tuition scholarship as well as travel costs and a stipend for living expenses for themselves and their families.

Qualifications: Applicants must have at least seven (7) years of public service experience in a field related to economic development or public policy. Mid-career professionals from all World Bank borrowing member countries, including former socialist countries, are eligible. The MPP Program at Princeton University is highly competitive. Successful candidates demonstrate both high professional achievement and exceptional academic records, including strong grounding in quantitative and economic analysis.



Chief of Party

Catholic Relief Services (CRS) is seeking a Chief of Party to manage a five-year USAID-funded southern Sudan Agriculture Revitalization Program for a multi-partner consortium. The program will focus on agricultural production, marketing, training in agribusiness development and agricultural technology, strengthening commodity network groups and construction of agricultural training centers.

Qualifications include:

- Advanced degree in Agricultural Economics, Business Administration or a related agribusiness field
- Minimum of 8 years experience in management, planning and implementation of rural development or agriculture projects in a developing country
- Experience in business skills training and capacity building
- Knowledge of Arabic a plus

The position is based in southern Sudan (non-family post), with frequent travel to Nairobi. For further details and application information, please visit our website at www.catholicrelief.org and refer to the JOBS section. Indicate salary requirements in your cover letter and refer to Req. No. I 02 025, Source Code ECON, ceo

Catholic Relief Services
209 West Fayette Street, Baltimore, MD USA 21201-3443



fewer forum on early warning and early response

FEWER is an independent global network committed to peace-building by providing coordinated responses to violent conflict. The Secretariat in London is seeking an:

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Responsibilities include co-ordinating the FEWER network, leading a dedicated team of staff, strategic planning, fund-raising, financial management and raising the profile of the network. The successful candidate will have a minimum of seven years senior management and leadership experience in an international institution, extensive knowledge of early warning, and three years experience in conflict affected countries. He/she will also have demonstrable experience in raising funds for humanitarian, developmental, or peace building initiatives.

Closing date: 23 October 2002. For details and an application form, see www.fewer.org, send a large stamped addressed envelope to Natasha Jolob, FEWER, Old Truman Brewery, 91-95 Brick Lane, London E1 6QN, or e-mail: njolob@fewer.org.

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Tenders

SCIENCE TECHNOLOGY AND INNOVATION

Establishment of Strategic Advisory Panel 2002-2004.

Victoria is a south-eastern State of Australia. It accounts for over 25% of the nation's GDP despite being only 3% of the Australian landmass.

The Department of Innovation Industry and Regional Development (IIRD) is the primary agency charged with facilitating the State's economic development.

The Science, Technology and Innovation (STI) division of IIRD supports the ongoing development of a scientifically and technologically advanced Victoria. The Government recognises that technological and scientific innovation is central to the State's future development. The Government has committed AUD\$310 million over 5 years to support new activities that build Victoria's science and technology base and foster innovation and commercialisation.

The Department seeks to identify a panel of individuals that they may engage to provide strategic advice in relation to commercialisation and development of emerging technology industries in the State of Victoria. The first stage of the process is to approve tenderers to a panel for possible future engagement at agreed conditions. The second stage will be the engagement of individual panellists on an as-needed basis dependent on projects the Government wishes to pursue between 2002 and 2004. There is no provision for retainer payments of panellists who are unengaged.

The panel will encompass a diversity of experience and approaches to industry development and innovation. Respondents will be individuals with demonstrated expertise in strategic, policy and technical advice in industry development of emerging technology-based sectors and the establishment of an optimal environment for the commercialisation of innovation. They will have operated at the interface of government, industry and academia in an international context. Detailed selection criteria can be found in the Project Brief.

Project briefs are available from <http://www.tenders.vic.gov.au>, tender **STISAP01**, and interested parties may telephone James Seymour, STI, on **+61 3 9651 9111**.

Applications are required by 14:00, Australian Eastern Standard Time, **3 October 2002**.

Applications should be sent to Tender Box, Level 9, 55 Collins St, Melbourne, Victoria 3000, Australia.
Faxed or late proposals cannot be considered.



InnaBase 038353

Invitation for Expressions of Interest

from interested entrepreneurs/firms to participate in establishing Expo Centre at Lahore, Pakistan

The Government of Pakistan and the Government of Punjab have decided to establish a modern, state-of-the-art exhibition and fair centre at Lahore, the provincial capital of the most populous province of Pakistan. A modern metropolis, Lahore is the cultural and touristic centre of Pakistan. The city and surrounding areas offer visitors superb facilities and diverse attractions. The need to develop such a facility in Lahore was felt as more than 60% of exports from Pakistan originate from this region.

Therefore, this project would be designed to provide facilities under one roof to local exporters and foreign companies to exhibit their products, so that foreign trade delegations/buyers could be attracted to visit Lahore and get first hand knowledge of the products. The areas around Lahore comprise of clusters of industrial concerns that produce specialized quality products like sports goods, surgical instruments, cutlery, engineering goods and wooden furniture, apart from leather and textiles & clothing.

The idea of establishing this project has been visualised in the backdrop of the recent events whereby hitherto closed areas like Afghanistan and Central Asian Republics are expected to be opened for trade through land route. This area lies in close proximity to Afghanistan and CAR countries, as goods could be sent across the border in matter of hours. Therefore, this region is being seen as transit route as well as marketing hub for the countries of this region.

For this purpose, Government of Punjab has already earmarked a piece of land measuring 50 acres or 20.23 hectares at a prime location, which is easily accessible and has been provided with all civic amenities.

Expressions of Interest "EOI" are solicited from reputable international and/or local companies on either of the following basis latest by **October 15, 2002**: -

1. Possibility of equity participation by any internationally recognised company/consortium interested in managing this Expo Centre who has experience in this line of business, as one of the shareholders.
2. Possibility of participation by an internationally recognised company/consortium already in the business of management, running and marketing of such projects on BOT basis.
3. Possibility of participation by an internationally recognised company interested in operating the Expo Centre on lease or rental basis.
4. Any other arrangement for participation in the management and / or financing of the Expo Centre.

The EOI documentation furnishing information on nature and status of the entity, nature and scope of present business activities, relevant experience, financial profile, proposed participation arrangement(s) alongwith terms and conditions, etc., accompanied by draft/banker's cheque for US \$ 200 as processing fee (non-refundable) drawn in favour of Export Promotion Bureau, Government of Pakistan, may please be sent at the below-mentioned address.

To progress further, pre-qualified companies / consortia would be asked to furnish their detailed proposals for the chosen option(s) based on the Terms of Reference which will then be provided by the Convener.

The Government of Pakistan and the Steering Committee responsible for overseeing the establishment and management of the Lahore Expo Centre reserves the right to accept or reject any "EOI" by any company that has expressed such an interest without assigning any reasons.

For clarification / additional information, contact:

Kamal Shahryar
Executive Director (ESDC)



Export Promotion Bureau - Government of Pakistan

Mezzanine Floor, Block A, Finance and Trade Centre, Shahra-e-Faisal, Karachi, Pakistan
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Overview

Global **stockmarkets** shuddered this week on worries about the faltering economic recovery and its impact on corporate profits. America's Dow Jones Industrial Average fell by 4.8% over the week. European markets were hit much harder: Frankfurt slumped by 13% to its lowest since February 1997; Paris fell by 12% and London by 8%. Tokyo alone bucked the trend, with a small gain over the week, after the Bank of Japan announced on September 18th that it planned to buy shares directly from banks. By helping banks to reduce their huge equity portfolios, the central bank hopes to shield them from further falls in the stockmarket, which hit a 19-year low earlier this month.

America's industrial production unexpectedly fell by 0.3% in the month of August, the first decline this year. As a result, capacity utilisation in American factories dropped to 76%. The trade deficit narrowed in July, which should help to boost third-quarter GDP growth. However, the 12-month deficit widened to \$439 billion. America's overall current-account deficit rose to a record 5% of GDP in the second quarter.

Fears about Europe's wobbly recovery were ignited by news that **French** industrial production fell by 1% in July, leaving it down by 1.7% from a year ago. This follows last week's figures showing a similar fall of 1% in Germany in July. **Germany's** ZEW survey of business expectations fell in September to its lowest level in eight months.

Consumer-price inflation remains lower than a year ago everywhere in our table except Japan, where prices continue to fall. America's 12-month rate of consumer-price inflation rose to 1.8% in August, but largely because of a big jump in the prices of energy and tobacco. Britain's headline rate of inflation fell to 1.4% in the same month. The underlying rate, which strips out home-mortgage payments, fell to 1.9%, well below the Bank of England's 2.5% target

Switzerland's GDP increased by 0.1% in the second quarter after four consecutive quarters of decline. With both inflation and interest rates well below 1%, many economists are worried that the country is moving dangerously close to deflation.

Data on more countries are available to subscribers on www.economist.com

Output, demand and jobs

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production latest	Retail sales (volume) latest	Unemployment % rate	
	1 qtr*	1 year	2002	2003			latest	year ago
Australia	+ 2.4	+ 3.8 Q2	+ 4.0	+ 3.7	+ 4.3 Q1	+ 6.3 Q2	6.2 Aug	6.8
Austria	+ 0.3	- 0.6 Q1	+ 0.9	+ 2.4	+ 2.5 Jun	- 0.2 May	4.2 Jul	3.6
Belgium	+ 0.8	+ 0.3 Q2	+ 1.1	+ 2.7	+ 3.8 Jul	- 4.2 Jun	12.0 Aug†	11.6
Britain	+ 2.4	+ 1.2 Q2	+ 1.7	+ 2.9	- 2.5 Jul	+ 5.0 Aug	5.2 Jul†	5.1
Canada	+ 4.3	+ 3.2 Q2	+ 3.3	+ 3.4	+ 1.3 Jun	+ 6.3 Jun	7.5 Aug	7.3
Denmark	+ 4.4	+ 2.2 Q2	+ 1.6	+ 2.3	- 1.6 Jul	+ 4.1 Jun	5.1 Jul	5.1
France	+ 2.0	+ 1.0 Q2	+ 1.3	+ 2.6	- 1.7 Jul	+ 3.5 Aug	9.0 Jul††	8.7
Germany	+ 1.1	+ 0.1 Q2	+ 0.6	+ 2.2	- 2.0 Jul	- 1.7 Jul	9.9 Aug§	9.3
Italy	+ 0.9	+ 0.2 Q2	+ 0.8	+ 2.4	- 5.4 Jun	- 0.8 Jun	9.0 Apr	9.5
Japan	+ 2.6	- 0.7 Q2	- 0.5	+ 1.0	+ 3.3 Jul	- 4.8 Jul	5.4 Jul	5.0
Netherlands	+ 0.5	+ 0.1 Q2	+ 0.9	+ 2.4	- 3.0 Jun	- 2.1 May	2.3 Aug**	2.0
Spain	+ 1.8	+ 2.0 Q2	+ 2.0	+ 2.9	+ 1.8 Jul	na	11.3 Jul	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.8	+ 2.7	- 1.3 Jun	+ 4.7 Jul	4.3 Jul†	4.2
Switzerland	+ 0.4	- 0.4 Q2	+ 0.9	+ 2.2	- 8.8 Q1	+ 1.7 Jul	2.7 Aug†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.5	+ 3.0	+ 0.4 Aug	+ 6.3 Jul	5.7 Aug	4.9
Euro area	+ 1.4	+ 0.6 Q2	+ 1.0	+ 2.4	- 1.2 Jun	- 0.9 Jun	8.3 Jul	8.0

*% change at an annual rate. †Not seasonally adjusted. ‡May-July; claimant count rate 3.1% in Aug. §EU harmonised rate 8.3% in Aug.

**Jun-Aug. ††Revised series.

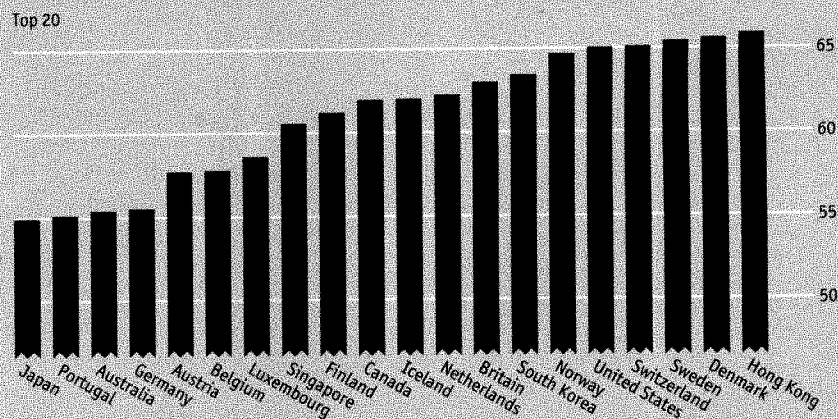
Prices and wages

% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2002	2003	latest	year ago	latest	year ago
Australia	+ 2.8 Q2	+ 6.0	+ 2.8	+ 2.5	- 1.1 Q2	+ 5.6	+ 3.7 Q2	+ 4.4
Austria	+ 1.9 Aug	+ 2.5	+ 1.7	+ 1.7	- 0.6 Aug	+ 1.7	+ 2.4 Jul	+ 2.8
Belgium	+ 1.3 Aug	+ 2.7	+ 1.7	+ 1.5	+ 0.8 Aug	- 1.0	+ 2.6 Q2	+ 2.6
Britain	+ 1.4 Aug	+ 2.1	+ 1.9	+ 2.4	+ 0.3 Aug	+ 0.2	+ 4.0 Jul	+ 4.6
Canada	+ 2.1 Jul	+ 2.6	+ 1.8	+ 2.2	- 0.3 Jul	+ 0.8	+ 3.0 Jun	+ 1.5
Denmark	+ 2.3 Aug	+ 2.5	+ 2.3	+ 2.0	- 0.3 Aug	+ 1.5	+ 3.7 Q2	+ 4.7
France	+ 1.8 Aug	+ 1.9	+ 1.8	+ 1.4	- 1.5 Jun	+ 2.3	+ 3.8 Q2	+ 4.2
Germany	+ 1.1 Aug	+ 2.6	+ 1.4	+ 1.2	- 0.5 Aug	+ 1.5	+ 2.5 Jun	+ 1.9
Italy	+ 2.4 Aug	+ 2.8	+ 2.3	+ 1.8	+ 0.1 Jul	+ 1.3	+ 2.2 Jul	+ 2.5
Japan	- 0.8 Jul	- 0.8	- 0.9	- 0.5	- 1.3 Aug	nil	- 5.6 Jul	+ 0.7
Netherlands	+ 3.3 Aug	+ 4.7	+ 3.6	+ 2.4	- 0.4 Jul	+ 2.4	+ 3.0 Jul	+ 5.1
Spain	+ 3.6 Aug	+ 3.7	+ 3.3	+ 2.6	+ 0.6 Jul	+ 2.0	+ 4.0 Q1	+ 3.4
Sweden	+ 2.0 Aug	+ 3.1	+ 2.3	+ 2.0	- 0.8 Jul	+ 2.1	+ 2.9 Jun	+ 2.8
Switzerland	+ 0.5 Aug	+ 1.1	+ 1.0	+ 1.2	- 1.4 Aug	- 0.2	+ 2.5 2001	+ 1.3
United States	+ 1.8 Aug	+ 2.7	+ 1.6	+ 2.2	- 1.6 Aug	+ 2.0	+ 3.1 Aug	+ 4.1
Euro area	+ 2.1 Aug	+ 2.7	+ 2.1	+ 1.6	- 0.6 Jul	+ 2.1	+ 3.3 Q1	+ 2.8

The mobile telecommunications and Internet index*, 2002

In a new report, the International Telecommunication Union (ITU) ranks more than 200 economies according to their performance in mobile telecommunications and Internet technologies, as well as their ability to take advantage of future developments in these fields. In all, 26 indicators covering the quality and extent of network infrastructure, network usage and market conditions were used to construct the ITU's index.



Source: International Telecommunication Union

*Maximum 100, minimum 0

Money and interest rates

	Money supply*			Interest rates % p.a. (Sep 18th 2002)					
	% change on year ago			3-mth money market		2-year		10-year gov't bonds	
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	corporate bonds
Australia	- 4.1	+ 9.4	Jul	4.95	4.38	4.99	5.47	5.56	6.73
Britain	+ 8.6	+ 5.8	Aug	3.94	4.56	3.71	4.41	4.88	5.64
Canada	+17.2	+ 7.2	Jul	2.82	3.18	3.41	4.86	5.23	6.85
Denmark	+ 6.2	+10.2	Jul	3.40	4.13	3.61	4.54	5.05	6.85
Japan	+31.5	+ 3.5	Aug	0.02	0.01	0.00	1.22	1.37	1.13
Sweden	+ 2.2	+ 4.2	Jun	4.13	3.73	4.32	4.81	5.14	4.80
Switzerland	+12.0	+ 5.8	Aug	0.73	2.75	0.63	2.51	3.20	3.75
United States	+ 3.2	+ 8.3	Aug	1.77	2.76	2.01	3.85	4.69	6.32†
Euro area†	+ 7.6	+ 7.1	Jul	3.31	3.76	3.18	4.29	4.76	5.13

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. ‡Sep 11th. Benchmarks: US 30-year 4.75%, Japan No.241 1.23%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.002%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholm Börsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Stockmarkets

Market indices

	Sep 18th	2002		% change on			
		high	low	one week	record high	Dec 31st 2001 in local currency	in \$ terms
Australia (All Ordinaries)	3,070.7	3,440.0	2,937.8	- 0.9	-10.7	- 8.6	- 2.2
Austria (ATX)	1,090.3	1,357.2	1,090.3	- 3.7	-37.2	- 4.4	+ 5.0
Belgium (Bel 20)	2,015.0	2,899.8	2,001.6	-10.9	-45.3	-27.6	-20.5
Britain (FTSE 100)	3,865.4	5,323.8	3,777.1	- 8.2	-44.2	-25.9	-21.1
Canada (Toronto Composite)	6,304.8	7,958.1	6,161.1	- 4.7	-44.6	-18.0	-17.4
Denmark (KBX)	172.5	233.4	169.0	- 7.8	-42.8	-23.3	-15.7
France (SBF 250)	2,038.3	3,081.9	2,038.3	-10.3	-53.6	-31.6	-24.9
(CAC 40)	3,001.0	4,688.0	3,001.0	-11.7	-56.6	-35.1	-28.8
Germany (Xetra DAX)	3,124.9	5,462.6	3,124.9	-12.8	-61.3	-39.4	-33.5
Italy (BCI)	1,101.4	1,513.0	1,077.8	- 6.1	-49.5	-23.2	-15.6
Japan (Nikkei 225)	9,472.1	11,979.9	9,075.1	+ 0.8	-75.7	-10.2	- 3.1
(Topix)	927.8	1,139.4	886.4	+ 1.2	-67.8	-10.1	- 3.0
Netherlands (AEX)	316.1	531.2	316.1	-14.0	-55.0	-37.6	-31.5
Spain (Madrid SE)	622.7	848.1	622.7	- 7.7	-45.7	-24.5	-17.1
Sweden (Affarsvarlden Gen)	142.0	236.8	142.0	- 7.8	-64.5	-38.6	-30.9
Switzerland (Swiss Market)	4,814.5	6,694.1	4,607.8	- 8.3	-42.8	-25.0	-17.0
United States (DJIA)	8,172.5	10,635.3	7,702.3	- 4.8	-30.3	-18.5	-18.5
(S&P 500)	869.5	1,172.5	797.7	- 4.4	-43.1	-24.3	-24.3
(Nasdaq Comp)	1,252.1	2,059.4	1,206.0	- 4.8	-75.2	-35.8	-35.8
Europe (FTSE Eurotop 300)*	863.6	1,279.7	862.3	- 9.9	-49.4	-31.5	-24.8
Euro area (FTSE Eblor 100)*	713.9	1,125.1	713.9	-11.8	-54.0	-35.8	-29.5
World (MSCI)†	777.5	1,024.4	756.7	- 5.4	-46.3	na	-22.5
World bond market (Salomon)‡	496.4	504.2	430.3	+ 0.5	- 1.5	na	+12.9

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.

‡Salomon Smith Barney World Government Bond Index, total return, in \$ terms.

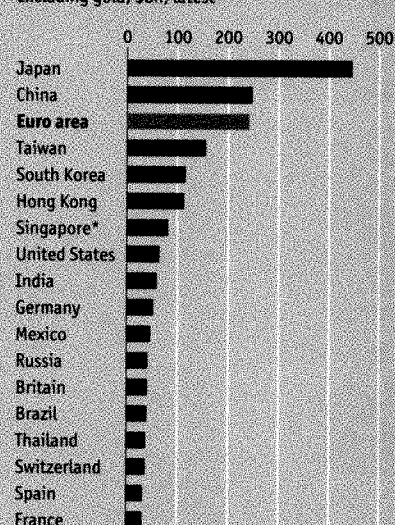
The Economist commodity price index 1995=100

	Sep 10th	Sep 17th*	% change on one month	% change on one year
Dollar index				
All items	76.5	75.5	+ 3.9	+13.3
Food	81.9	81.5	+ 7.3	+18.9
Industrials				
All	69.0	67.5	- 1.3	+ 5.2
Nfa†	71.3	69.3	- 3.2	+10.2
Metals	67.1	65.9	+ 0.6	+ 1.0
Sterling index				
All items	77.7	77.6	+ 3.3	+ 7.9
Euro index				
All items	103.2	102.5	+ 4.6	+ 7.8
Yen index				
All items	97.4	98.4	+ 6.9	+18.2
Gold				
\$ per oz	318.20	316.60	+ 2.6	+10.1
West Texas Intermediate				
\$ per barrel	29.64	29.11	- 2.4	+ 4.9

* Provisional. † Non-food agriculturals.

Official reserves

Excluding gold, \$bn, latest



Sources: IMF; national statistics

*Includes gold

Trade, exchange rates and budgets

	Trade balance*, \$bn latest 12 months		Current account				Exchange rate		Currency units					Budget balance % of GDP 2002‡				
			\$bn latest 12 mths		The Economist poll % of GDP, forecast 2002 2003		trade-weighted† Sep 18th year ago		per \$		per £	per euro	per ¥100					
									Sep 18th	year ago								
Australia	-	1.3	Jul	-	11.6	Q2	-	3.7	-	3.8	73.6	67.6	1.83	2.02	2.83	1.78	1.50	0.1
Austria	-	1.4	Jun	-	0.9	Jul	-	2.2	-	1.9	na	100.5	1.02	1.08	1.58	-	0.84	-0.3
Belgium	+	15.1	Jun	+	11.8	Mar§	+	5.0	+	5.1	na	99.5	1.02	1.08	1.58	-	0.84	nil
Britain	-	44.9	Jul	-	31.2	Q1	-	2.1	-	1.9	106.3	104.7	0.65	0.68	-	0.63	0.53	-0.8
Canada	+	34.3	Jul	+	12.1	Q2	+	2.1	+	2.2	75.0	76.2	1.59	1.57	2.46	1.55	1.31	1.0
Denmark	+	7.1	Jul	+	3.3	Jul	+	1.9	+	1.8	102.8	103.2	7.60	8.01	11.8	7.43	6.26	2.2
France	+	10.2	Jul	+	27.3	Jul	+	1.7	+	1.6	na	102.2	1.02	1.08	1.58	-	0.84	-2.0
Germany	+	104.5	Jul	+	30.2	Jul	+	1.2	+	1.0	na	99.2	1.02	1.08	1.58	-	0.84	-2.8
Italy	+	9.8	Jun	-	3.2	Jun	-	0.1	-	0.0	na	72.9	1.02	1.08	1.58	-	0.84	-1.4
Japan	+	83.8	Jul	+	110.9	Jul	+	2.9	+	2.9	133.6	141.8	121	117	188	119	-	-8.0
Netherlands	+	25.0	Jul	+	2.7	Q2	+	3.9	+	4.0	na	98.5	1.02	1.08	1.58	-	0.84	0.1
Spain	-	36.4	Jun	-	15.3	Jun	-	2.1	-	1.8	na	74.6	1.02	1.08	1.58	-	0.84	-0.3
Sweden	+	14.7	Jul	+	8.1	Jul	+	3.2	+	3.2	77.6	72.3	9.32	10.5	14.4	9.11	7.67	2.1
Switzerland	+	3.5	Aug	+	25.7	Q1	+	10.0	+	10.2	114.1	112.2	1.50	1.59	2.33	1.47	1.24	na
United States	-	438.5	Jul	-	428.8	Q2	-	4.5	-	4.1	114.6	115.6	-	-	1.55	0.98	0.82	-1.0
Euro area	+	79.2	Jun	+	24.8	Jun	+	0.5	+	0.5	81.5	80.1	1.02	1.08	1.58	-	0.84	-1.5

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast. §New series.

Overview

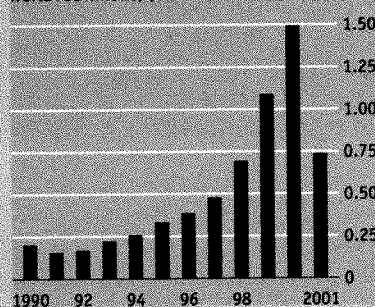
Many analysts feared that **China's** economy would slow in the second half of 2002, after growing at an annual rate of 7.8% during the first six months of the year. But, so far, fears that exports (a good indicator of China's economic growth) would drop have proven unfounded. In the year to August, exports rose by 25%; industrial production rose by 12.7%. In other good news, consumer-price deflation eased slightly.

Inflation, not deflation, is becoming a problem for **South Africa**. Consumer prices rose by 11.6% in the year to August, the highest rate of inflation since 1992.

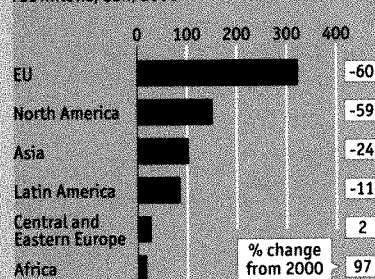
Foreign direct investment

After reaching record levels in 2000, foreign direct investment (FDI) declined sharply in 2001. The slump was concentrated in the world's rich countries, where the frantic pace of cross-border mergers and acquisitions flagged after years of growth. FDI flows to the European Union shrank by 60%, while North America's inflows slowed by 59%. FDI into Africa almost doubled, although from a modest base, rising from \$9 billion in 2000 to over \$17 billion in 2001. But most of this investment was concentrated in a few big projects in South Africa and Morocco. In the emerging markets, Argentina, Brazil and Hong Kong suffered a combined \$57 billion decline in inbound FDI. In 2001, America continued to attract more FDI than any other country; it also invested the most abroad of any country.

World FDI inflows, \$trn



FDI inflows, \$bn, 2001



Source: UNCTAD

Economy

	% change on year ago			Latest 12 months, \$bn		Foreign reserves* \$bn, latest
	GDP	Industrial production	Consumer prices	Trade balance	Current account	
China	+ 8.0 Q2	+12.7 Aug	- 0.7 Aug	+29.1 Aug	+17.4 2001	246.8 Jun
Hong Kong	+ 0.5 Q2	-11.6 Q1	- 3.4 Jul	- 8.2 Jul	+14.1 Q1	112.3 Aug
India	+ 6.4 Q1	+ 6.4 Jul	+ 3.9 Jul	- 5.1 Jul	+ 1.4 Q1	58.3 Aug
Indonesia	+ 3.5 Q2	- 9.4 Q4	+10.6 Aug	+27.3 Jul	+ 6.1 Q1	29.5 Jul
Malaysia	+ 3.8 Q2	+ 6.9 Jul	+ 2.1 Aug	+13.4 Jul	+ 7.0 Q1	32.8 Jul
Philippines	+ 4.5 Q2	+ 5.9 Jun	+ 2.9 Aug	+ 2.8 Jul	+ 6.2 May	13.4 Aug
Singapore	+ 3.9 Q2	+17.8 Jul	- 0.4 Jul	+ 6.4 Jul	+17.5 Q2	80.9 Aug
South Korea	+ 6.3 Q2	+ 8.9 Jul	+ 2.4 Aug	+ 9.8 Aug	+ 5.3 Jul	115.4 Jul
Taiwan	+ 3.0 Q2	+11.4 Jul	- 0.3 Aug	+18.6 Aug	+24.8 Q2	155.3 Jul
Thailand	+ 5.1 Q2	+ 9.6 Jul	+ 0.3 Aug	+ 3.8 Jul	+ 6.5 Jul	37.0 Jul
Argentina	-16.3 Q1	- 9.6 Aug	+36.5 Aug	+13.4 Jul	nil Q1	9.0 Jul
Brazil	+ 1.0 Q2	+ 3.3 Jul	+ 7.5 Aug	+ 7.4 Aug	-16.7 Jul	39.1 Jul
Chile	+ 1.7 Q2	+ 8.6 Jul	+ 2.2 Aug	+ 2.4 Aug	- 0.6 Q2	15.0 Jul
Colombia	+ 2.2 Q2	- 1.2 Jun	+ 6.0 Aug	+ 0.5 Jun	- 1.4 Q1	10.6 Jul
Mexico	+ 2.1 Q2	+ 1.9 Jul	+ 5.3 Aug	- 9.1 Jul	-16.3 Q2	46.1 Jul
Peru	+ 3.8 Jul	+ 6.8 Jul	+ 0.1 Aug	+ 0.2 Jul	- 1.0 Q2	9.2 Jul
Venezuela	- 9.9 Q2	-17.1 Jun	+24.0 Aug	+ 8.5 Q2	+ 1.9 Q2	7.6 Jun
Egypt	+ 4.9 2001†	+ 7.8 2001†	+ 2.7 Jun	- 8.2 Apr	- 0.1 Q1	12.6 May
Israel	- 1.7 Q2	+ 1.6 Jun	+ 6.2 Aug	- 6.3 Jul	- 2.3 Q1	24.5 Aug
South Africa	+ 2.2 Q2	+ 7.8 Jul	+11.6 Aug	+ 3.1 Jul	- 0.3 Q2	6.0 Jul
Turkey	+ 2.3 Q1	+12.3 Jul	+40.2 Aug	-10.3 Jun	+ 2.0 Jun	23.2 Jul
Czech Republic	+ 2.5 Q2	+10.8 Jul	+ 0.6 Aug	- 2.5 Jun	- 2.3 Q2	21.6 Aug
Hungary	+ 3.1 Q2	+ 5.1 Jul	+ 4.5 Aug	- 2.4 Jul	- 2.1 Jul	10.3 Jul
Poland	+ 0.5 Q1	+ 6.0 Jul	+ 1.2 Aug	-10.4 Jul	- 6.4 Jul	27.1 Jul
Russia	+ 4.1 Q2	+ 3.4 Aug	+15.2 Aug	+42.4 Jul	+28.3 Q2	40.6 Aug

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Financial markets

	Currency units		Interest rates	Stockmarkets	% change on		
	per \$	per £			Dec 31st 2001	in local currency	in \$ terms
	Sep 18th	year ago	Sep 18th	Sep 18th	one week		
China	8.27	8.28	12.8	na	1,664.1	-1.6	- 2.8 - 2.7
Hong Kong	7.80	7.80	12.1	1.88	9,474.1	-4.1	- 16.9 - 16.9
India	48.4	48.0	75.0	5.72	3,069.8	-1.8	- 5.9 - 6.2
Indonesia	9,000	9,605	13,944	14.50	419.1	-2.6	+ 6.9 + 23.5
Malaysia	3.80	3.80	5.89	3.20	677.2	-1.8	- 2.7 - 2.7
Philippines	52.3	51.4	81.0	6.75	1,153.3	-0.0	- 1.3 - 2.6
Singapore	1.77	1.74	2.75	1.19	1,431.3	-1.2	- 11.8 - 8.2
South Korea	1,208	1,297	1,872	4.82	703.9	-2.9	+ 1.5 + 10.3
Taiwan	34.6	34.6	53.7	2.10	4,482.7	-3.8	- 19.2 - 18.4
Thailand	42.9	44.2	66.5	2.00	354.0	-2.0	+ 16.5 + 20.0
Argentina	3.63	1.00	5.62	39.10	378.0	-2.1	+ 28.0 - 64.7
Brazil	3.35	2.71	5.19	17.90	9,505.4	-6.6	- 30.0 - 51.7
Chile	730	691	1,131	2.64	4,843.2	-1.3	- 10.3 - 18.8
Colombia	2,788	2,343	4,320	7.96	1,202.7	+0.0	+ 12.3 - 8.3
Mexico	10.02	9.40	15.5	6.99	5,960.4	-4.8	- 6.5 - 14.4
Peru	3.60	3.49	5.58	4.27	1,162.3	-1.8	- 1.1 - 5.4
Venezuela	1,450	743	2,246	29.90	7,390.9	+2.7	+ 12.5 - 41.2
Egypt	4.64	4.26	7.18	7.13	5,291.7	+1.0	+ 0.4 - 1.0
Israel	4.79	4.32	7.41	6.40	354.9	-2.2	- 20.6 - 26.8
South Africa	10.6	8.64	16.4	13.05	9,582.1	-3.6	- 8.2 + 4.0
Turkey	1,667,750	1,504,000	2,583,845	42.00	9,257.5	-0.1	- 32.8 - 41.4
Czech Republic	31.0	37.0	48.0	3.00	445.1	-1.9	+ 12.8 + 29.6
Hungary	249	278	386	9.69	7,438.7	-2.5	+ 4.3 + 15.1
Poland	4.16	4.20	6.44	7.94	13,063.7	-2.6	- 6.2 - 10.8
Russia	31.7	29.5	49.1	21.00	329.8†	-4.9	+ 31.7 + 26.8
EMF (MSCI)*	1.00	1.00	1.55	na	284.6	-4.4	na - 10.3
EMBI+†	1.00	1.00	1.55	na	204.4	-1.8	na + 2.0

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In \$ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; UBS Warburg; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; Russian Economic Trends.

Data on more countries are available to subscribers on www.economist.com



WHEN WE DECIDED
TO DEVELOP A
CLEANER FUEL,
FERRARI
GAVE US A
HEAD START.

Clive McDonald and his Shell Fuels Research team have been actively involved in the development of racing fuels for many, many years now.

Creating high performance grades that have driven, and continue to drive, the world of F1 to greater heights.

However, this relentless search for fuels that power the likes of Ferrari hasn't been to the detriment of the urban motorist. In fact, it has actually led to cleaner, greener fuels capable of greatly reducing CO₂ emissions.

Which has the proven potential to significantly lessen these emissions in cities around the world.

In effect, it represents the creation of a forest more than 100 times the size of Manhattan.

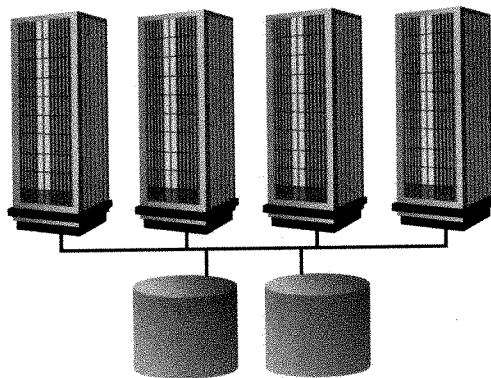
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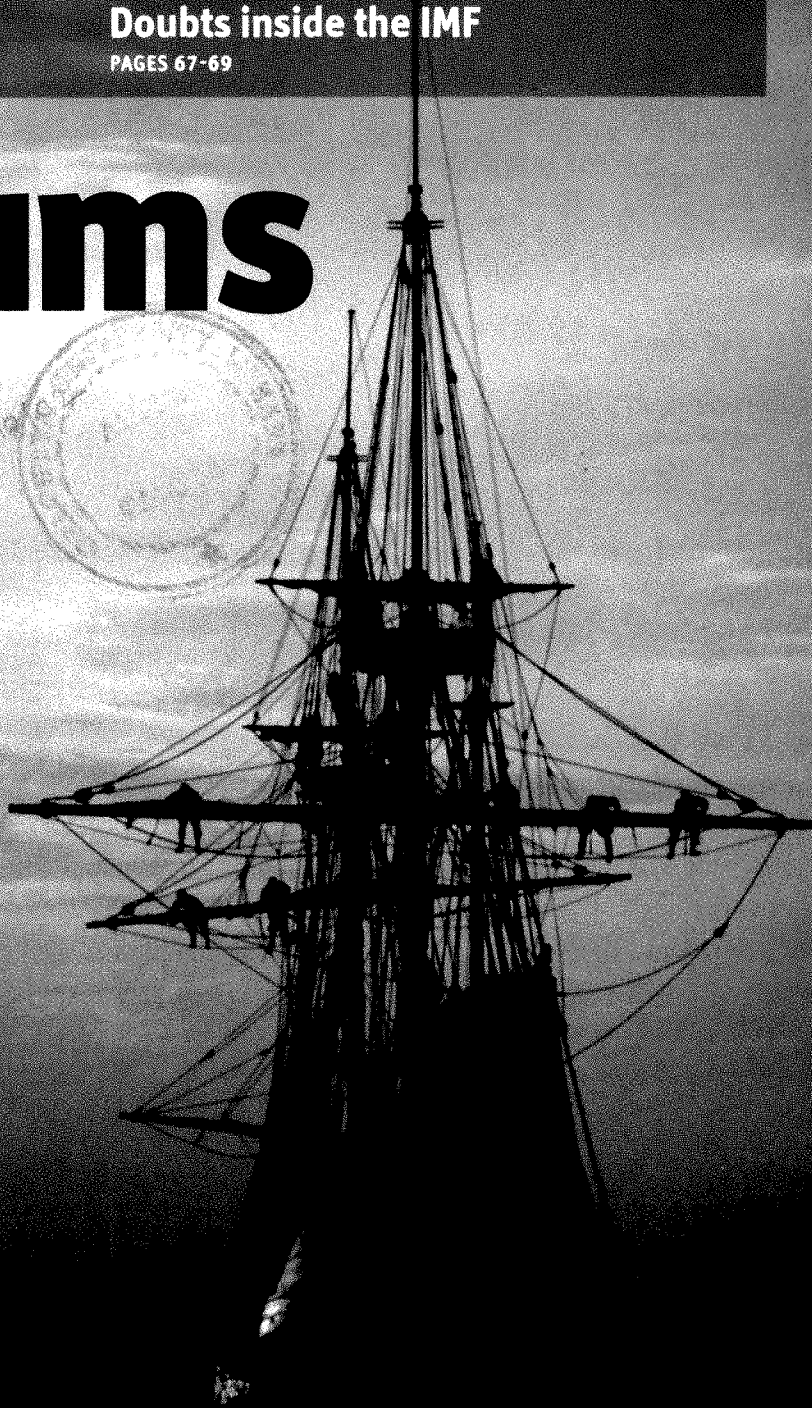
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Doldrums

The world
economy
and how to
rescue it

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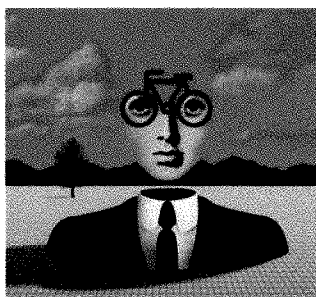
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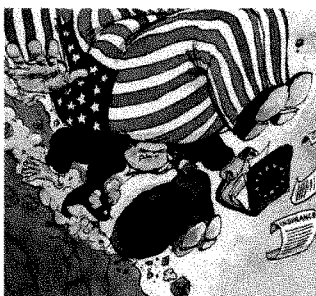
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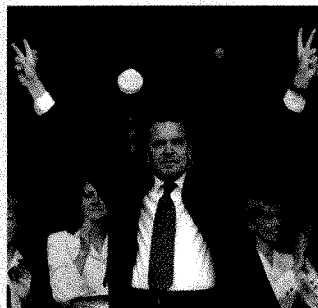
Politics

The Bush administration published a new **National Security Strategy**, pledging to work with allies but also emphasising that "to forestall or prevent...hostile acts...the United States will, if necessary, act pre-emptively." Al Gore, the former vice-president, attacked both the doctrine of pre-emption and the administration's apparent determination to attack Iraq, saying it was damaging both the effort to fight terrorism and America's alliances.

Gray Davis, the governor of California, signed a bill allowing scientists in his state to use embryonic **stem cells** for research, defying federal restrictions on the practice.

According to the Census Bureau, the proportion of Americans in poverty (living on less than \$18,104 a year for a family of four) rose last year by 0.4 percentage points to 11.7%, the first rise for eight years.

Schröder scrapes in



Germany's chancellor, Gerhard Schröder, and his ruling coalition of Social Democrats and Greens narrowly won re-election, beating the conservative Christian Democrats and their Bavarian sister party, the Christian Social Union, led by Edmund Stoiber, by a handful of seats. The Greens tipped the balance by winning nearly 9% of the vote, a point ahead of the Free Democrats, Germany's liberals, who were thought more likely to team up with the conservatives.

Donald Rumsfeld, America's defence secretary, said that relations between the United

States and **Germany** had been "poisoned" by the vehemence of Mr Schröder's refusal to let Germany join an attack against Iraq, even under a UN mandate, and by the alleged comparison of George Bush with Hitler by Germany's justice minister.

Russia appeared to soften its opposition to the drafting of a new UN resolution on Iraq after its foreign minister, Igor Ivanov, said that his government was prepared to discuss the issue. America said that Iraq had helped al-Qaeda to develop chemical weapons.

Slovakia's ruling centre-right coalition combined to defeat the country's former strongman, Vladimir Meciar, who nonetheless topped the poll in a general election with 20%. The country now looks set to join NATO and the EU.

In Spain's **Basque** region a civil guard was killed by a booby-trap planted by members of the separatist terror group, ETA. A day earlier two ETA members blew themselves up when explosives in their car went off accidentally.

Fighting violence

Over 3,000 soldiers were sent to the western state of Gujarat, in **India**, in an effort to prevent widespread violence after suspected Islamic militants killed over 30 people in a Hindu temple. In February, inter-communal violence in the state left thousands of Muslims dead after an attack on a train carrying Hindus.

Nineteen people, including five security personnel and nine suspected Islamic militants, died in violence after the second round of voting for the state assembly in Indian-administered **Kashmir**. Only 11% of voters turned out in Srinagar, the Muslim-majority city at the centre of the insurgency against Indian rule.

Unidentified gunmen shot dead seven Pakistani employees of a Christian charity in Karachi in **Pakistan**. Attacks on Christians elsewhere in the

country have killed more than 30 people in the past year.

A government offensive in **Nepal** against Maoist rebels saw more than 150 insurgents killed. The offensive came in response to recent rebel attacks on army barracks and police stations in which around 100 security personnel died.

Concerned that the transitional administration of Hamid Karzai could not cope, **Afghanistan's** minister for refugees asked Britain and other European countries not to force asylum-seekers back to the war-ravaged country.

An **Indonesian** human-rights organisation concluded that army special forces were probably behind the killing of two Americans and an Indonesian in Papua province in August. The army had blamed separatist rebels for the attack.

America said it will soon dispatch an envoy to **North Korea**. The reclusive state has embarked on a diplomatic charm offensive.

Hurricane force



After battering Cuba, hurricane Isidore hit the Yucatan peninsula in **Mexico**, killing at least three people and forcing tens of thousands out of their homes.

Intensifying its war against the country's rebels, the government of **Colombia** established "security zones", giving the military sweeping powers to re-establish the authority of the state. The measure coincides with a visit to Washington of the country's new president, Alvaro Uribe, who is seeking more help.

Argentina's government said "the world won't end" without an IMF aid deal. Repayments, however, could. Roberto Lavagna, the economy minister, said an IMF package was the only way to avoid defaulting on repayments to multilateral lenders.

Arafat's diminishing base



After last week's suicide bomb in Tel Aviv, the Israeli army demolished all but one of the buildings in **Yasser Arafat's** Ramallah headquarters, besieging him and 200 others in the remaining wing. George Bush called Israel's action "unhelpful" and America abstained as the UN Security Council passed a resolution calling on Israel to stop its military operation in Ramallah and to withdraw expeditiously from the Palestinian cities it occupies.

Fighting continued in **Côte d'Ivoire** after an attempted coup. American troops flew in to help the French garrison protect foreigners, including 20,000 French citizens and 170 American children trapped in a mission school in Bouaké, a rebel-held town.

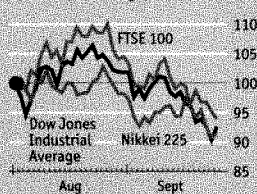
Talks aimed at securing a ceasefire in **Burundi** failed after the main rebel group could not even agree on terms under which its representatives might meet with the government.

The late Nigerian dictator **Sani Abacha's** son, Mohammed, was released from jail, where he had been detained since 1999 on corruption charges. He was freed reportedly on condition that he return most of the \$1.5 billion his father is estimated to have stolen.

Business

Down market

Stockmarkets, August 1st 2002–100



More bad times for the world's **stockmarkets**. America's Dow Jones and Nasdaq continued down as worries about the economy and rising oil prices took hold. Before rallying on September 25th, Britain's FTSE 100 hit a six-year low. Germany's Xetra Dax Index fell after Gerhard Schröder's narrow victory in weekend elections.

The Federal Reserve left interest rates unchanged but voiced growing concerns over the slow rate of **America's economic recovery**. Alan Greenspan, the Fed's chairman, arrived in Britain to receive an honorary knighthood for his efforts at maintaining economic stability.

The IMF added to the gloom. Its *World Economic Outlook* suggested that the **world economy** is recovering only slowly. Estimates for America's growth this year were cut to 2.2% and slashed for 2003. The Fund now expects the world economy to grow by just 3.7% in 2003, down from 4%.

The EU's "**growth and stability pact**", the supposed rock on which the euro's credibility is founded, suffered tremors. As the euro area's big economies (France, Germany and Italy) together with Portugal looked likely to breach the pact's upper limit for fiscal deficits of 3% of GDP, the European Commission decided to extend by two years (to 2006) the deadline for balanced budgets. The Union's smaller countries complained: they had made stringent efforts to meet the deadline.

The **Bank of Japan** added to the amazement caused by its decision to buy shares from banks with an admission that it was "an independent decision based on a serious concern about the state of the financial system" and was intended as a "catalyst" to spur action by government and regulators on the banks' mountainous bad-loan problem. It also admitted that the new policy was "a big gamble".

Fischer overboard
Citing "differences of opinion", Leonhard Fischer abruptly quit as chief executive of the loss-making corporate- and investment-banking arm of Germany's **Dresdner Bank**. Although Mr Fischer has sacked his fellow investment bankers by the hundreds, Dresdner still has to deal with its high corporate-banking costs.

Goldman Sachs reported profits for the third quarter of \$522m, up by 12% on a year ago, as money from trading offset a decline in income from mergers and acquisitions at the American investment bank. Trading activities suffered at **Lehman Brothers**, Goldman's poor relation, propelling its profits down by 37% in the third quarter, to \$194m.

The top brass at **AMP** paid the price for the company's poor performance and plunging share price. The chief executive of the Australian insurance firm will depart at once, the chairman in six months' time.

Citigroup's investment bank, **Salomon Smith Barney**, was fined \$5m by American regulators for issuing misleadingly bullish research about Winstar Communications, a now bankrupt telecoms company that was also a client of the bank. Regulators also filed a complaint against Jack Grubman, once Salomon's star telecoms analyst, and his former assistant, the authors of the research in question.

Universal strategy
Vivendi Universal set out long-awaited plans to reduce its prodigious debt pile. It plans to sell assets worth up to €12 billion (\$11.8 billion), and confirmed that its publishing businesses would go. But the French media giant gave little indication of the future of its stakes in Vivendi Environnement, a utility, or Cegetel, a French telecoms firm; rumours abounded that both would be sold. It also announced a board shake-up; six members resigned.

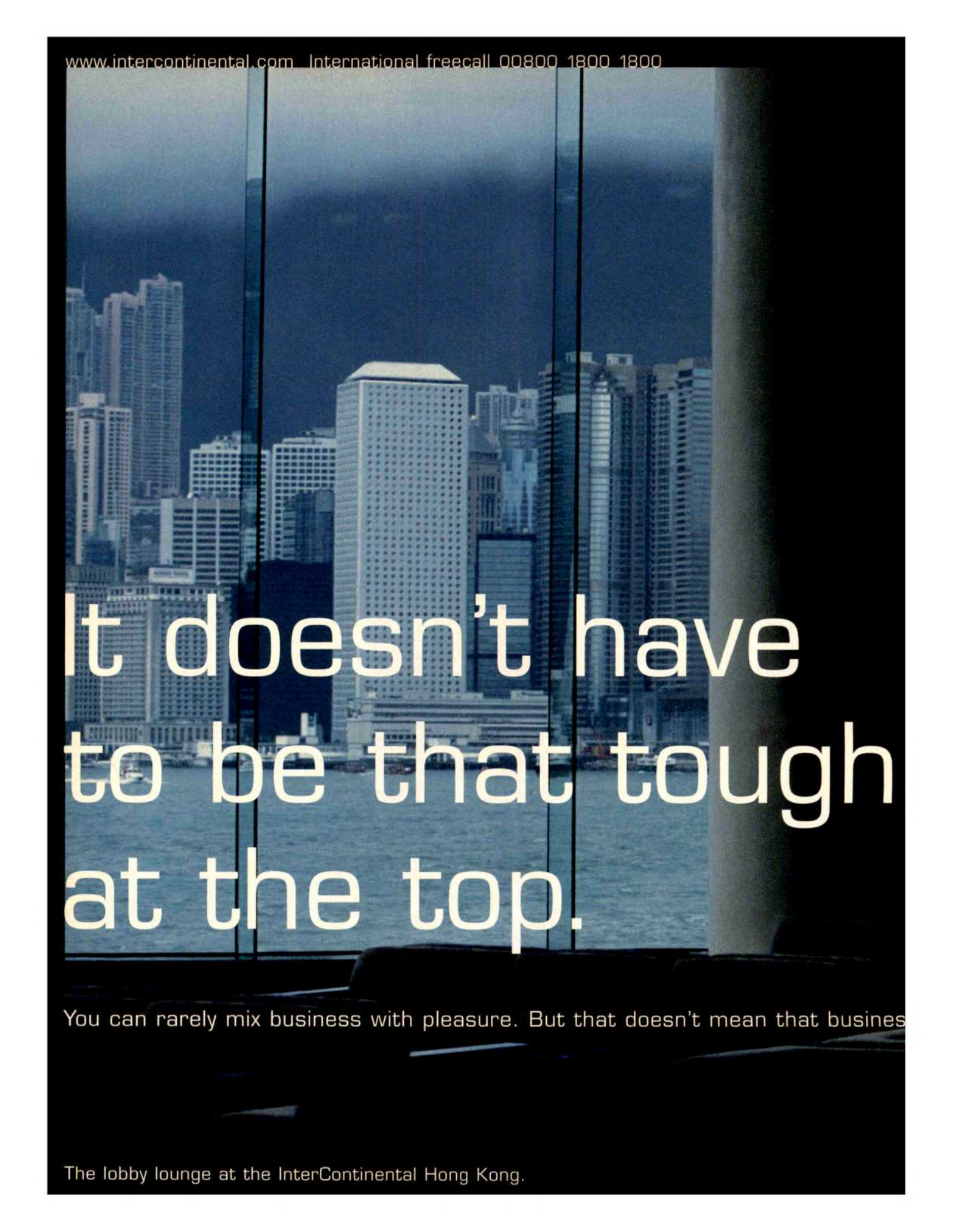
Alcatel, a struggling French telecoms-equipment maker, raised some much needed cash by selling a stake of just over 6% of Thales, a French defence company. It will raise some €340m (\$333m) while retaining some 10% of Thales. Days before, Alcatel had predicted a bad year and announced 10,000 jobs cuts, some 14% of its total employees, before the end of 2003.

Bad copy?
Xerox faced a criminal investigation arising from suspicions that it had inflated its profits. In April, the heavily indebted copier company was fined \$10m after a probe of its accounting practices by America's Securities and Exchange Commission revealed widespread abuse. Xerox says it has cleaned up its act.

America's energy regulators strongly hinted that they blame energy companies for **California's energy crisis** of 2000-2001. A ruling that subsidiaries of El Paso, a gas company, had restricted supply during the crisis suggests that it and others will shoulder the blame—and be made to cough up—for the power problems.

Other economic data and news can be found on pages 104-106

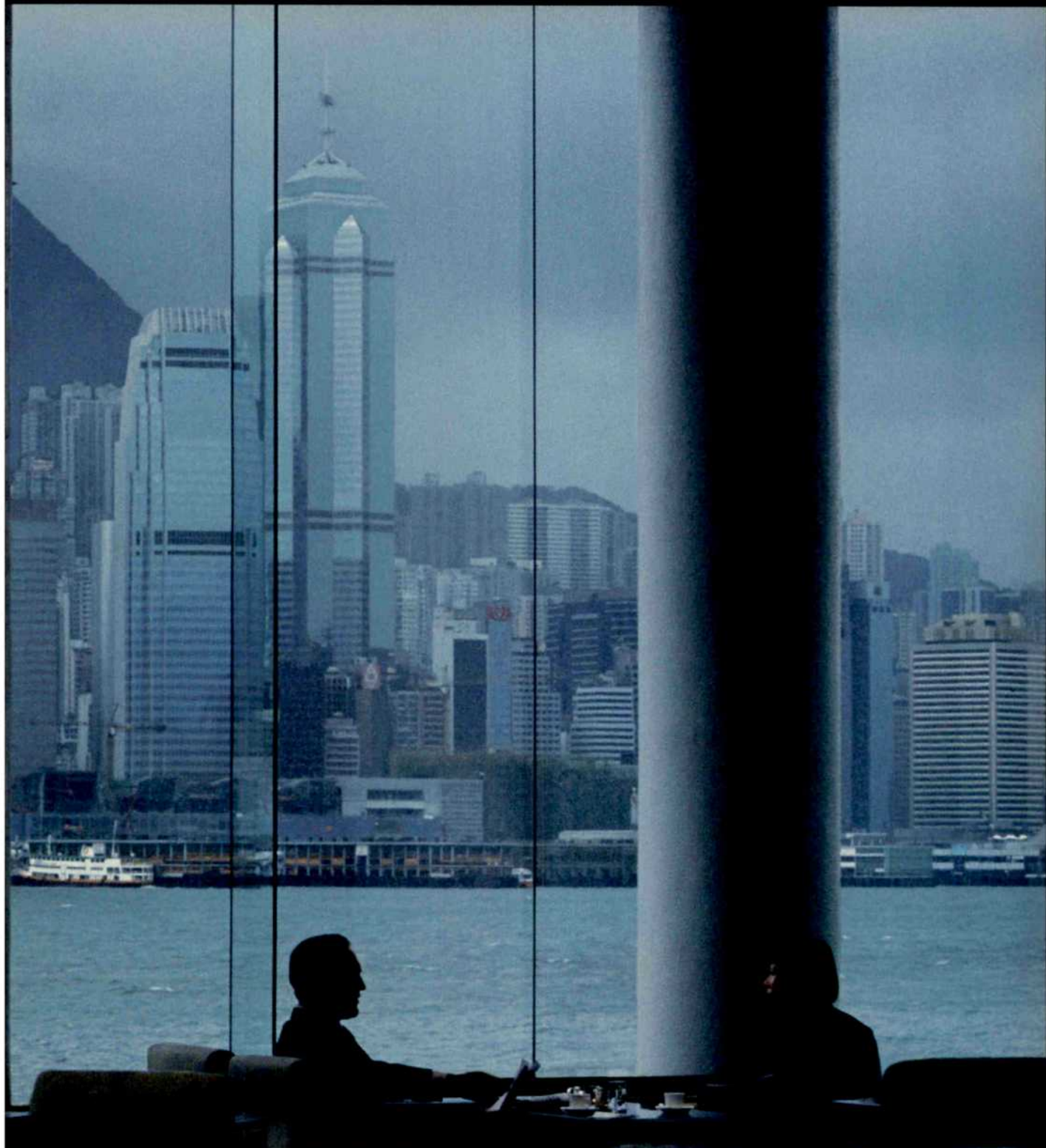




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How to rescue it

The world economy is in the doldrums. Both monetary and fiscal policy need to be put to work



CENTRAL bankers are popularly portrayed like ships' captains carefully steering their economies. In reality, central bankers have more in common with the early navigators: they often don't know where they are, let alone where they are

heading; their maps and compasses are unreliable and their steering is wonky. Worst of all, their recent policy dilemmas are the equivalent of not knowing whether the earth is round or flat. Today's central bankers learnt their trade in a world where the main danger was inflation. But in recent years, the biggest hazards have instead been asset-price bubbles and now, perhaps, deflation. As shares slump and economies wobble, the world's top economic policymakers meeting this weekend for the annual meetings of the IMF and the World Bank (see pages 67-69) will be asking whether the navigators can now rescue the world from its current doldrums.

Most American economists reckon that their economy is under way again after being halted last year: they typically expect growth to return to trend or above during the next 12 months. They still do not grasp that this recession was quite different from all previous post-war cycles. It followed the bursting of the biggest financial bubble in American history. Share prices have since seen their biggest fall since the Great Depression. During the bubble years, decisions across the whole economy—about investment, borrowing and saving—were distorted by unrealistic expectations about future profits and share prices, and a belief that the business cycle was dead. The latter was particularly foolish: our survey in this issue argues that not only is the cycle likely to turn bumpier in future, but America's current downturn is far from over. The economy is unlikely to return to vigorous and sustained growth until the excesses created by the bubble have gone. Consumers continue to borrow as if little has changed, encouraged by low interest rates and rising house prices. But debts cannot rise faster than incomes for ever; eventually households will need to save more and spend less, which implies several years of slow growth or even a double-dip recession.

The other big economies are in no better shape. Japan's grew in the second quarter, but it remains fragile and deflation continues unabated. The Bank of Japan's desperate plan to buy shares from banks (see page 72) is unlikely to help, especially as there is plainly no coherence in the plan nor any clear policy response from the finance ministry either. In the euro area domestic demand is virtually flat; most of its pathetic growth over the past year has come from exports. Share prices, which have fallen by even more from their peak than on Wall Street, are depressing consumer and business confidence in Europe by more than in the past. Germany's GDP may now be shrinking again. Add to this fragile global mix the risk that military action against Iraq will push up oil prices temporarily and further reduce share prices, and the outlook looks bleak.

So why did America's Federal Reserve not cut interest rates this week? It faces a dilemma. On the one hand, America's

economy needs a period of below-trend growth to eliminate its financial excesses. This argues against a rate cut, which would only encourage consumers to borrow even more, exacerbating America's financial imbalances and simply postponing the day of reckoning. On the other hand, a weak economy at a time when inflation is already low (1% as measured by the GDP deflator), could lead to deflation. This argues for aggressive monetary easing.

One way out of this dilemma would be a sharp fall in the dollar, which would allow America to unwind its imbalances without a recession. A cheaper dollar would boost exports to offset weaker domestic spending and also prevent deflation by lifting import prices. The snag is that this would export deflation to Japan and Europe, and neither appears to be able or willing to bring about an offsetting economic stimulus. That appearance, though, is deceptive.

Turn on the engines

Even if the big economies do not actually slip back into recession, global growth is likely to remain well below trend, which will cause inflation to fall further. There is therefore a risk that by the end of next year the big three economies, America, Germany and Japan, will all have falling prices. History suggests that central banks should do everything they can to avoid deflation, which is far more harmful than inflation, especially when economies are awash with debt. But today's policymakers, trained to fight inflation, are ill prepared. Japanese interest rates are already at zero and the Fed does not have much ammunition left, with rates at a 40-year low of 1.75%. The European Central Bank (ECB) has the most room to cut rates (currently 3.25%), but its telescope is so keenly searching for any hint of inflation on the horizon that it is oblivious to deflationary icebergs floating by. The ECB's inflation target of "less than 2%" is also too low; it provides an inadequate cushion against the risk of deflation in the event of a serious slump in demand.

The current monetary-policy risks are lop-sided. If a cut in rates turns out to have been unnecessary, it can easily be reversed; and with ample spare capacity there is little risk of inflation soaring. On the other hand, once deflation sets in, nominal interest rates cannot normally fall below zero, so there is no way to deliver the negative real interest rates that may be needed to pull an economy out of recession. The lesson from Japan is that the Fed and the ECB should cut interest rates soon. Another lesson, though, is that as rates approach zero and monetary policy starts to feel like "pushing on a string", as Keynes argued, fiscal policy needs to play a bigger role.

Instead there is currently much debate in America, Japan and the euro area about the need to cut budget deficits to prevent the build-up of unsustainable public debts. That would be folly, grand scale. At the very least, built-in fiscal stabilisers (the automatic fall in tax revenues and rise in jobless benefits as economies weaken) should be allowed to operate fully. Europe's fiscal stability pact, in particular, foolishly prevents this. If a government's deficit breaches 3% of GDP it can be automatically forced to tighten policy even if the economy is in recession. That now seems likely to happen to Germany. This ▶▶

► week the European Commission proposed to relax a deadline the pact had set for budgets to balance; this would be welcome but is nowhere near enough. The euro members need to loosen their fiscal straitjacket immediately and rewrite the stability pact to take account of the cycle. Some argue that to rewrite the pact now would hurt the euro's credibility. But it is far worse to stick to a lousy policy than to admit it is wrong and change it. Ask Argentina.

Admittedly, discretionary fiscal fine-tuning has a poor record. It is hard to get the timing right and in normal circumstances it seems less effective in boosting demand than was once thought. Deflation, though, is highly abnormal. If monetary policy becomes impotent, a budgetary stimulus is the only weapon left. Contrary to popular opinion, fiscal stimulus has worked in Japan when it has been tried. But Japan's true stimulus has been much more modest than the increase in its budget deficit would suggest. Most of the increase in borrow-

ing has been due to a fall in tax revenues as GDP has shrunk. It is not too late for Japan to fight deflation by pursuing a proper fiscal reflation, which could be financed by the Bank of Japan buying government bonds. If the Bank refuses to do that then the finance ministry should do its own reflation by intervening in the currency markets to drive down the yen.

All around the world, extra measures are needed. Only two years ago, Alan Greenspan, the Fed's saintly navigator, believed America's economy was heading into a new world of faster growth and higher profits. Instead it looks horribly like the old world before 1939 when financial bubbles and investment-led booms always eventually ended in bust. Somehow or other, America needs to rid itself of its financial excesses, and it is in that sense that America's "recession" is far from over. If the world economy is to get moving again, it is time not only for the Fed to cut interest rates but also for Europe and Japan to turn on their engines. Doldrums are dangerous. ■

American foreign policy

Pre-empting threats, threatening pre-emption

Only Saddam Hussein, and any would-be emulators, need fear George Bush's foreign policy



MUCH of the time, foreign policy is made by hints, bribery, threats and, in this televisual age, soundbites. This week it was made in a pair of substantial documents—America's new "National Security Strategy", outlining George

Bush's foreign-policy thinking, and the British government's "assessment" of Iraq's weapons of mass destruction. The first was intended to reassure, the other to scare. The truly scary thing is that much of the reaction to these documents—in soundbites, naturally—has got them the wrong way round.

Mr Bush's "strategy", which is the sort of thing every administration gets round to assembling, contained nothing seriously new (see page 35). What caught the attention, though, was one element that had been mentioned before but not fully fleshed out: the notion that, if America saw that a country or organisation was developing nuclear, chemical or biological weapons for use against it, then it would be willing to take pre-emptive action to deal with that threat. In other words, it would not wait until thousands or millions of people had been killed. Such action need not only mean war, the report stressed, and would not necessarily be done by America alone. But if a unilateral military strike were absolutely necessary, then Mr Bush said he was willing to order one.

The question is: should you be scared by that, or reassured? First of all, some distracting arguments need to be cleared away. This does not, as some say, set a "precedent" for future invasions by any Russia, China or, indeed, Iraq. Despite the fine words of the United Nations Charter deploring the use of force, dozens of its signatories have used "pre-emptive" attacks during the past half-century: the Soviet Union on many occasions, Israel, Iraq, many African countries, India, Pakistan and the United States itself (in Grenada, for example), among others. And how good it would have been for the world, most people still think, if the democracies had pre-empted Hitler

back in the mid-1930s. Second, it does not entail America giving itself new "rights" or flouting existing sources of "legitimacy": all Mr Bush has said is that, in *extremis*, he will act. So would many other countries, in their own extremity.

First and foremost, this is reassuring to Americans: if someone is building a suitcase nuclear bomb to be exploded in Chicago, the president will not wait for years of debate and piles of reports from international study-groups before doing something to stop it. Yet it should also reassure other people. They should be reassured by the promise that such a move is very much a last resort. But they should also be reassured by America's willingness to threaten it. For the point of the threat is old-fashioned deterrence: that by declaring your willingness to act, you will make it less likely that you will ever need to act. Such deterrence, in so far as it works, will help protect others too—especially as America, both in its general values and explicitly in this document, stands for freedom and democracy, not imperial conquest or dictatorship.

Saddam Hussein: a worked example

In the end, the basic issue is whether you trust America to act more-or-less wisely, or whether you think it (or Mr Bush personally) is in fact a Wild West cowboy. Given the careful, determined response Mr Bush gave to the terrorist attacks on September 11th, and given the fact that for all the words about "regime change" he has done nothing precipitate against Iraq, it is hard to find any evidence of cowboy tendencies, at least on his part. It ought also to be reassuring that his new security strategy is packed to the brim with idealistic language about peace and prosperity for all, and full of declarations of intent to work with allies, reinforce non-proliferation treaties, operate through multilateral organisations and so on.

But should you believe such words? Scepticism is always in order when a government speaks, especially when strategy documents thud into the world's awkward realities. Iraq does, though, offer a case-study in how things might work. For it is hard to imagine a better current example of when to consider ►►

► pre-emptive action as an alternative to containment: a murderous dictator and declared enemy of America who has been building stockpiles of chemical and biological weapons for 20 years, and is trying to develop nuclear weapons too.

However, far from blundering unilaterally into an invasion on a presidential whim, Mr Bush has placed the United Nations at the heart of his strategy against Saddam Hussein. His closest ally, Britain, this week laid out in painstaking detail the evidence of Mr Hussein's weapons programmes, his deceit, his evasion of weapons inspections and his use of such weap-

ons in the past. The dossier (see page 56) contained only a few new facts but much that should be scary to those unfamiliar with Mr Hussein's past record. Now, Britain and America will try to persuade the Security Council to pass a new resolution threatening force unless Mr Hussein fulfils his past promises to disarm, which over the past 11 years have been the subject of 16 UN resolutions. The threat of invasion is being used as a last-but-one resort; the threat of a unilateral invasion is only a last resort. Mr Hussein, it is to be hoped, is now scared. On this evidence, nobody else needs to be. ■

British politics

The two Tonys

Is that world leader the same man as the British prime minister?



THERE'S something rather heroic about Tony Blair at the moment. Heroic and wrong, some would say; heroic and right, this newspaper would contend; but nobody would deny that it takes courage to face

down deep scepticism in your party, to see your natural allies in the press desert you and to watch your government's poll ratings slide—all for a policy which is unlikely to make a halfpenny-worth of difference to your performance in the next election.

The reason why Mr Blair cuts such an impressive figure these days is that he has total confidence in his moral and political instincts. He doesn't need focus groups or polls to tell him that his compass is true. The big tent has been packed up and put away, consensus-building is off the agenda and the Third Way is forgotten. The only way is Tony's way, and those who don't like it can lump it.

Yet however things go in Iraq, come the next election Mr Blair will be judged not on foreign policy, but, as he has asked to be, on whether or not people believe that he is delivering the improvements he has promised in key public services. And on this issue, Mr Blair cuts a very different figure. The single-minded courage with which he has pursued his aims abroad serves only to highlight the muddle-headedness and timidity which characterise his record at home. The results of the government's attempts to improve things (see page 55) are as unimpressive as Mr Blair's performance.

Take exams, for instance, a particularly hot topic this week. Without really thinking, Mr Blair has subscribed to the idea that headlong expansion of higher education is a good thing. He talks of "nobody being left behind" and the opportunity for everyone to fulfil their potential. The practical application of these pleasant sentiments is the government's determination to send 50% of the population to university. But without better secondary education, the only way of ensuring that enough students scrape the necessary A-levels to get to university is the new, dumbed-down, exam system for 18-year-olds. Predictably, it has resulted in catastrophe, with examiners apparently manipulating some students' marks downwards to conceal the dumbing-down. Voters are left with the impression not just that the government has been cheating their children, but that it has been doing so incompetently. And, as the

Tories learnt after Britain was spat out of the European exchange-rate mechanism ten years ago, there's nothing voters dislike so much as incompetence.

The National Health Service has escaped such spectacular disaster; but neither does it show any sign of improvement. The main flaw in the government's policy on health—and the other public services—is that it is spending without reforming. Although the NHS has seen its budget rise by a third since 1998, little has been done to encourage more competition to state-owned providers or to offer more choice to consumers. Power has been centralised, not devolved. Yet it is hard to find anybody who knows the NHS and seriously believes that an organisation employing a million people can be made to work. What's more, by pouring money into a fundamentally flawed system, the government is jeopardising its one real domestic achievement so far—not having messed up the economy.

The Falklands factor, again

Gordon Brown, the chancellor, does not see the need to dismantle the NHS or even decentralise power within it. Reform is best achieved through targets set by himself. So long as every doctor does what the Treasury tells her to, the system will work fine. Mr Blair has become uncomfortable with this belief in command and control—his proxy, the health secretary, Alan Milburn, has engaged in battle over the setting up of semi-independent "foundation" hospitals that Mr Milburn supports and Mr Brown opposes, for instance—but it's hard to tell, for Mr Blair rarely asserts himself domestically these days.

That has been especially true over the past few months, and not just because Mr Blair (rightly) thinks that current events abroad are of greater moment than those at home. It is also because Mr Blair, like any politician, has only a limited amount of political capital. When he is spending heavily on bringing doubters in line on Iraq, he has little to spare for the intractable business of public service reform.

That may change. The best hope for Britain is that Mr Blair's Iraq policy is a success, for he might then turn to domestic affairs with new vigour. That, after all, is what happened with Margaret Thatcher. Her most active period of reform came after she defeated aggressors abroad and doubters at home over the Falklands in 1982.

Mr Blair's performance over Iraq has shown how impressive a world leader he can be. It would be nice to have a British prime minister with that sort of energy and courage. ■

Hong Kong

Subverting autocracy

Plans for an anti-subversion law are not as bad as feared—but are still a big step in a very wrong direction



“THE well water should not interfere with the river water,” Deng Xiaoping once said, meaning that Hong Kong should not seek to meddle with China after it was handed back in 1997. Most of the concern had been the other way around: that

China might damage Hong Kong’s economic and political freedoms. Deng foresaw that a free-wheeling place like Hong Kong could hardly help but pose a challenge to China’s political rigidities. Sadly, though, he drew the wrong conclusion. So the Chinese authorities have long pressed Hong Kong to introduce laws that would outlaw any attempt to “subvert”—for which, read challenge—its system.

At last, the attempt has succeeded: the administration of Tung Chee-hwa this week released its proposals for a new raft of laws which will make it harder for Hong Kong to act as a focus for dissent in China (see page 29). The proposals, it is true, could certainly have been worse. The offences they define—treason, secession, sedition and subversion—all require the commission of, or the incitement to commit, acts of violence against people, property or services. Merely demonstrating peacefully for regime change or the independence of Taiwan, or writing newspaper articles encouraging either objective, will not get you banged up, as it surely would in China proper.

Still, nestling among the plans are a few more alarming aspects. An organisation (such as the exercise cult Falun Gong, to take a far from hypothetical example) could under the new plans be banned automatically by Hong Kong if China de-

cides that it is a threat to national security rather than just an “evil cult”, or if it finds a way to define it as a “political party”. The rules on disclosing official secrets are tightened. There is the suggestion that hacking into Internet sites could be construed as an act of violence. Inciting public disorder could become a crime.

Naturally, the Hong Kong government defends itself vigorously, explaining that its proposals are akin to those on the books in many other common-law countries. But there is something unpalatable about the attempt by the Hong Kong government’s lawyers to dress up what they are doing in the language of western governance. The precedents they rely on are of democracies taking what are acknowledged to be extreme reserve powers to protect themselves from the small risk of an attempt at overthrow by small but violent groups of extremists. Such powers are tightly controlled by the fact that their users must answer to voters and to independent courts.

The case of Hong Kong’s new laws is in each detail the reverse of that. The proposals Mr Tung’s administration has come up with have been pressed on him by Beijing in order to protect a self-appointed regime from highly probable attempts, which would be supported by the great mass of Chinese people, to secure the democratic rights enjoyed almost everywhere else in Asia. Such actions, moreover, are subject to very little control: Mr Tung has recently been reinstalled for another five years, without even the formality of a vote by Hong Kong’s Beijing-picked electoral college. And Hong Kong’s courts, as has already been established, are subject to reversal by China’s. An anti-subversion law is bad for Hong Kong and, in the end, is bad for China too. ■

Yasser Arafat

Arafat under siege, again

How not to change the Palestinian regime



IF THERE were a Yasser Arafat preservation society, Ariel Sharon and his men would be founder members. Their decision to mount a public performance to humiliate and threaten Mr Arafat interrupted an unprecedented revolt by

younger parliamentarians against their eternal leader. The result was predictable: instead of challenging Mr Arafat to give up his executive powers, Palestinians marched in his defence.

In slow motion, by the light of the television cameras, Israeli bulldozers spent last weekend destroying Mr Arafat’s Ramallah headquarters, leaving Mr Arafat and about 200 companions cowering in a single wing (see page 45). The timing of this action was so plainly counter-productive that the charitable suggested that it might be little more than an unthought-

out, emotional reaction to the horror of last week’s two suicide bombs in Israel, particularly the one in central Tel Aviv.

Yet the cat-and-mouse pursuit of Mr Arafat fits neatly into Israeli tactics that focus on the Palestinian leader and his failings. Mr Sharon has American backing for his refusal to deal with Mr Arafat. And since Israel’s prime minister, or so many suspect, would also prefer not to deal with any Palestinian if the bargaining were to lead him to a territorial concession, there is logic to keeping an enfeebled Mr Arafat in place. Meanwhile, the Israeli army continues its bid, as outlined by its chief of staff, to batter the Palestinians into capitulation.

But this, as Kofi Annan, the UN’s secretary-general, warned Israel this week, is a bankrupt policy that will not work. The Security Council then passed a resolution that called on Israel immediately to cease its military actions in Ramallah and “expeditiously” to withdraw its army towards the positions it held two years ago. Israel, as usual, took little notice. ►►

► This is embarrassing for America, which, with Iraq on its mind, would like to give the Arab world as little cause as possible to compare Israel's attitude to Security Council resolutions to that of Iraq's. Unusually, it abstained on the resolution, rather than vetoing it. But, despite the now rare phenomenon of American displeasure, Israel's siege of Mr Arafat's compound seems set to continue, and its military operations in Gaza are even intensifying.

The new crisis has temporarily blown away the Palestinians' demand for internal change. But it will return. Their parliament, deeply underwhelmed by Mr Arafat's new cabinet, had forced it to resign. Before fresh ministers could be appointed, the building they meet in had been turned to dust.

Elections are the answer

The Palestinians do not wish to follow Israeli-American instructions by unseating their leader. But they do want radical reform. By this, they mean a more competent administration, and a separation of powers between the Palestine Liberation Organisation (the umbrella theoretically sheltering all Palestinians) and the Palestinian Authority. Above all, they want President Arafat to appoint a prime minister—the compromise

candidate, acceptable to most, is Mahmoud Abbas, also known as Abu Mazen—to run the West Bank and Gaza.

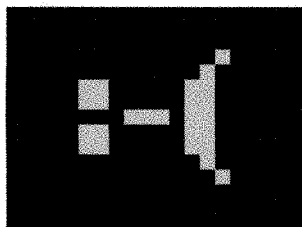
Mr Arafat's reluctance to relinquish authority is legendary. But he does at least say that he is not against the idea of a prime minister, in principle. He should be pushed hard, by friendly outsiders as well as by his own people, to turn principle into practice. Once he has conceded the change, the democratic way of putting it into effect would be at the elections he has promised for January 20th, but which can take place only if Israel releases the West Bank from its tight bonds of sieges, closures and curfews.

At present Israel's government, with America's encouragement, is determined not to allow elections that would benefit Mr Arafat. This is a mistake, and blatantly undemocratic. Although the old man would almost certainly be re-elected president, a free election would also bring in a larger number of younger, more representative parliamentarians. This is not the sort of regime change that the Americans, let alone the Israelis, might have chosen. But it will be a group more in tune than the old guard were with Palestinian aspirations. And if Mr Arafat has been persuaded to devolve most of his executive responsibilities, it will also be more competent. ■

3G telecoms

Let Europe's operators free

Far from extending their lead in wireless technology, over-regulation has destroyed it



EUROPE'S troubled wireless operators have two big problems. One is the familiar problem of debt, taken on to make pricey acquisitions during the technology bubble and to pay (more than €100 billion—\$90 billion) for licences to operate

“third generation” (3G) networks. The second problem is less familiar and more technical, but every bit as crippling.

Those expensive 3G licences require the operators to provide 3G coverage by certain deadlines. They also require that they do this using a particular technology, mandated by Europe's regulators at the behest of the European Commission. The technology, called W-CDMA, has just one big hitch: it doesn't work.

Sonera, Finland's national telecoms operator, switched on its fancy 3G network on January 1st. But nobody can use it. Sonera was supposed to launch its 3G services on September 26th via handsets provided by Nokia, the world's largest handset maker and Finland's biggest employer. But the launch was embarrassingly called off because the handsets do not work yet. In Austria, Mobikom, another 3G operator, launched its 3G network on September 25th, but with a very limited number of handsets. And in Britain, Hutchison 3G, another operator, will begin consumer trials of its 3G service next week, with a mere 1,000 sets.

The difficulty is that the W-CDMA handsets and networks made by different vendors do not yet work together properly. Most operators plan to use network equipment and handsets from several suppliers. Making sure that they all speak the same language looks likely to take another year or two. In the

meantime, it is hard to imagine why anyone in Europe would want to buy a 3G phone.

The decision to impose a single technological standard on Europe's operators was intended to reinforce the European lead in wireless technology. In practice, it has had the opposite effect. A recent report from Morgan Stanley concluded that Asia now leads in the adoption of 3G, followed by America. Europe is last. And why have Asia and America pulled ahead? Because they are using a different 3G technology, called CDMA2000, which actually works. Alas, European operators' 3G licences forbid them to use it.

The consumer's best interest

This month the European Commission agreed that 3G operators should be allowed to share sites for their base stations. The anti-competitive risks from co-operation between operators were deemed to be less important than the need to ensure a rapid roll-out of services. In other words, the regulators acknowledged their duty to act in consumers' best interests. Relaxing the technological straitjacket imposed on the operators would be further acknowledgement of that duty.

Admittedly, most of Europe's 3G licences were sold at auction. So granting refunds or relaxing the requirements could set a dangerous precedent for future auctions. But the licences are going to have to be amended anyway if operators cannot meet their deadlines to deliver 3G because they are forced to use a non-working technology.

So operators should be given the option to provide 3G services using technologies other than W-CDMA. Already, some of them are looking at switching to CDMA2000. Most will probably stick with W-CDMA while the bugs are ironed out. But they should at least have the freedom to choose. ■

Stopping Saddam

SIR – I wonder at the adverse reaction of many Europeans to the idea that America may go to war with Iraq (“Confronting Iraq”, September 14th). Saddam Hussein rules solely by fear, torture and murder. Even if Mr Hussein lets in inspectors to find and destroy weapons of mass destruction, Europe must ask itself whether he and the Baath oligarchy around him should be allowed to stay in power. Surely the free world owes it to the oppressed people of Iraq to rid them of this tyrant? Of course, this invites the question, “Why stop at Iraq?” There are plenty of murderous police-states in the world including most of Iraq’s neighbours, but one has to start somewhere.

NEIL WILSON
Cape Town

SIR – I agree that Mr Hussein must be replaced. However, wider issues should be addressed to ensure that a world after the demise of Mr Hussein is a safer one. For example, you overlook the fact that Iran is probably much closer to developing a nuclear bomb than Iraq. Also, what must be done to address the growing resentment of the Arab world as America consolidates its presence in the region?

ERICO TAVARES
Hong Kong

SIR – You assert that an attack on Iraq is justified by a need to counter Mr Hussein’s, as yet unseen arsenal. A much more convincing explanation is given in another article in the same issue entitled “Don’t mention the O-word”.

CHRIS GREACEN
Berkeley, California

Chinese wall

SIR – Your article on censorship of the Internet in China referred to an organisation backed by the Chinese government that calls itself the Internet Society of China (“Stop your searching”, September 7th). I want to make it clear

that this group is in no way affiliated to the Internet Society (ISOC), a global not-for-profit membership organisation founded in 1991 to provide leadership in Internet-related standards, education and policy development.

The attempt at censorship in China is diametrically opposed to our principles and we would never endorse a pledge to limit the dissemination of information nor similar actions that you describe. ISOC’s primary mission is to expand stable and secure use of the Internet worldwide and to encourage openness, transparency and democratic processes. Access to the Internet is an important ingredient in the free flow of information necessary for the long-term welfare of all countries. Government-imposed limitations on access to search engines, as proposed by China, serve neither citizens nor their governments.

LYNN ST AMOUR
President and CEO
Internet Society
Reston, Virginia

Globalisation and the poor

SIR – You rightly correct Thabo Mbeki’s gross factual distortion of the effects of the past decade of globalisation (“Sustaining the poor’s development”, August 31st). Rather than analyse the true costs and benefits of the rise in trade and economic development, Mr Mbeki sides with those whose battle against poverty targets the wealthy rather than the root causes of the problem: disease, illiteracy and ignorance.

What goes unmentioned is Mr Mbeki’s staggering hypocrisy. Until recently he denied the true cause of AIDS, and restricted HIV education and the distribution of anti-AIDS drugs to his fellow South Africans (even when offered freely by western companies). In doing so, he is more responsible than most for “the avoidable increase in human misery” for which he blames the developed world. That such gross detachment is reflected

in the attitudes of countless southern leaders and northern intellectuals is a measure of how far we have to go before the world’s poor are truly free from suffering.

PAUL RUSHTON
Vancouver

SIR – Farm subsidies in developed countries are a necessary and moral way to maintain the ability of a state to feed its people. Without a strong agricultural economy no nation, no matter how powerful, can sustain itself for the long term. The fact that farmers in developing countries can produce and sell foodstuffs at a cheaper price is irrelevant. Developed countries would be foolish to let their farm economies disappear because of the presence of cheap imported food. Food, like oil or any commodity, can be controlled. As the world discovered during the 1970s and 1980s, those who control the supply of a particular commodity have shown no compunction about wielding that power like a club.

I do not mind paying taxes to keep America’s farmers farming, steel mills humming and shipyards in business. The ability to sustain liberty and independence demands nothing less.

MARK CARBONARO
Salinas, California

SIR – If sensible environmental policies are to come about, we need to cost damages and price restoration. As with statistics monitoring poverty, disease and corruption we might find that frequent publication of environmental data would be a further measure to hold politicians accountable.

STEFAN WALDBURGER
London

Fair share for the future

SIR – I am glad that you think I do a good job of analysing the pensions crisis in my book “Banking on Death” (“Matters of life and death”, August 31st). However, I would like to take issue with the criticism that the share levy I propose is

unfeasible since “any company faced with the prospect of being stripped of 20% of its profits would go and accumulate elsewhere.”

In fact, a share levy does not strip profits from a company, even though the new shares are calculated as a proportion of company profit. As far as the company is concerned its cash-flow is unaffected. So is the size of the dividend it chooses to distribute. What is changed is simply the composition of the recipients of those dividend payments, which will now include the national-pension board. Thus a share levy is not the same as a corporation tax, with the latter representing a “seizure of profits” (though this is sometimes passed on to consumers through higher prices). The great advantage of a share levy is that it yields income in the future, when pension needs are set to rise steeply.

If we look at the rival approaches to pension reform now before the United States Congress we find that it is the Republicans who propose that companies should be allowed to contribute shares to their employees’ retirement funds. It is the approach of Senator Edward Kennedy, which seeks to steer corporations towards cash contributions, that is deemed less business-friendly.

ROBIN BLACKBURN
New York

Hitting the right note

SIR – The mention of Louis Armstrong in your obituary of Lionel Hampton (September 7th) brought to mind the finest epitaph I have ever heard. One of Armstrong’s fellow jazz musicians said of him, “Louis was born poor, died rich and never hurt anybody.”

JAMES WATERS
Wilmington, North Carolina ■

Letters are welcome and should be addressed to the Editor at The Economist, 25 St James’s Street, London SW1A 1HG. Fax: 020 7839 2968 E-mail: letters@economist.com

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NHS Trust

Chief Executive

SALARY NEGOTIABLE/LOCATION: CHELSEA AND HAREFIELD, MIDDLESEX

The Trust is the UK's leading post-graduate specialist centre for heart and lung medicine, surgery and research with an international reputation. Following over six successful years, Mark Taylor, the Chief Executive, is due to retire on 31 March 2003 and the Trust is seeking his successor.

Reporting to the Trust's Board, the Chief Executive is responsible for a budget of £145 million and for over 2,000 employees. He/she will help define and drive a strategy that maintains and enhances the Trust's position at the leading edge of heart and lung medicine. Delivering the planned move of the Royal Brompton and Harefield

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Executive Focus

EMIRATE of ABU DHABI
THE WORKS DEPARTMENT



امارة أبوظبي
دائرة الأشغال

- Head of Administration
- Head of Finance
- Head of Audit & Control

The Works Department, Abu Dhabi Emirate, is seeking highly qualified candidates for the above positions in the immediate future. The long-term posting will be based at The Works Department, Abu Dhabi in the United Arab Emirates.

Pre-requisites for all the above positions are 20 years work experience (English a must, Arabic desirable). Eligible candidates are invited to send their CVs, supported by references, qualifications and employment history of current and past work experience by fax or email. Only short listed candidates will be contacted for interviews.

The Works Department was reorganised by an Emiri decree in 1975 with the objective of executing a development plan in the field of buildings, transportation, services and other government facilities and projects for the Emirate of Abu Dhabi to meet its social and economic development requirements.

The Department's total staff strength is 1700+, and its objectives and responsibilities (covering Abu Dhabi, Al Ain and the Western region areas), are as follows:

- Study, design, execution and maintenance of government building projects.
- Study, design, execution and maintenance of transportation and services projects.
- Carry out survey works and laboratory works related to buildings and roads and execution and maintenance of earth and rock roads projects.
- Assisting other government bodies in practicing its specialisation in respect to the development plan execution.
- Other responsibilities entrusted to the Department by The Executive Council of Abu Dhabi.

The major divisions of the Department are:

- Government Building Projects (Design and Execution Sections).
- Technical Affairs & Transport (Ports, Airports, Roads and Services Management).
- Technical Services (Maintenance & Minor Projects Management).
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EUROPEAN CENTRAL BANK

The European Central Bank (ECB), established in Frankfurt am Main on 1 June 1998, is seeking to fill the vacancy detailed below in the Operations Analysis Division, Directorate General Operations.

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ECONOMIST

(Ref.: ECB/101/02/I/TE)

Within the Operations Analysis Division of the Directorate General Operations, the Liquidity Management Unit, where the position is vacant, is responsible for the following activities: management of the global liquidity position of the banking system and preparation of monetary policy operations, assessment of the developments in the short term segment of the money market, conduct of analytical work related to the liquidity management and to the operational implementation of monetary policy, monitoring and maintenance of the Eurosystem's reserve requirement system.

The position holder will be involved in the following tasks of the Liquidity Management Unit of the Operations Analysis Division:

- Structural analysis and supervision of various aspects of the Eurosystem's liquidity management, including all related institutional aspects of the operational framework, such as the minimum reserve system and issues relating to Eurosystem counterparties.
- Regular analysis of the liquidity situation in the banking sector of the euro area.
- Preparation of proposals for monetary policy operations.

Qualifications and experience

- Advanced university degree in finance or economics or proven ability to perform the tasks commensurate with such formal academic qualification.
- Practical knowledge of financial markets and banking, experience with analytical work relating to monetary and financial issues, knowledge of central bank policies and operations.
- Ability to work in a team and under time pressure.
- Ability to communicate, both orally and in writing, complex issues in non-technical terms.
- Ability to identify and address policy issues.
- Good knowledge of statistical and economic methods.
- Very good command of English with proven drafting ability. A working knowledge of at least one other official Community language is required.

Applications

Applications should be submitted in English and include a covering letter, curriculum vitae and a recent photograph, together with references confirming the required experience and skills. They should be addressed, quoting the reference number, to the **European Central Bank, Directorate Human Resources, Postfach 16 03 19, 60066 Frankfurt am Main, Germany** and should reach the ECB no later than **18 October 2002**. Applications will be treated in the strictest confidence and will not be returned.

This vacancy has also been posted on the ECB's website at www.ecb.int. To meet the deadline, a copy may be sent by fax to +49 69/1344 7979 or by e-mail to recruitment@ecb.int. However, a signed application must still be sent by post.

International Monetary Fund

For its headquarters in **Washington, D.C.**, the **International Monetary Fund (IMF)** is seeking a:

Writer/Analyst

The selected candidate will attend meetings of the Executive Board, the Board of Governors, and their committees and prepare succinct reports and comprehensive formal records of the discussions. These discussions focus on economic and financial issues in member countries and the world economy, as well as on IMF policies and operations. The selected candidate will also prepare briefings on related background material before the meetings and will follow up on the Board's deliberations and decisions.

REQUIREMENTS: A graduate degree in economics or international relations is highly desirable. Previous writing and editing experience on financial and economic subjects is preferred. Candidates must have a good understanding of macroeconomic concepts and an interest in contemporary international economic issues; they must possess excellent writing skills and the ability to analyze, summarize, and present results precisely and logically within tight deadlines; and they must exercise good judgment and strong diplomatic skills. Short-listed candidates will be required to take a writing test.

Qualified candidates are invited to apply online through the IMF's website at www.imf.org/recruitment by **October 20, 2002**, making specific reference to **Vacancy Number R02353B**.

Further details about the role and function of the IMF are provided on its website:

<http://www.imf.org>



Executive Director

Six figure package



Montreal, Canada

World's largest trading bloc...the North American Free Trade Agreement (NAFTA) signed by Canada, Mexico and the United States created the North American Commission for Environmental Cooperation (CEC), an international organization to facilitate cooperation and public participation to foster conservation protection and enhancement of the North American environment for present and future generations. The CEC is composed of a council of cabinet-level environment officials from the three countries, the Joint Public Advisory Committee (a group of five citizens from each country) and a Secretariat staffed with environmental experts.

Lead and direct...the operations of the Secretariat. Report to the CEC Council. Play a key role in the development of strategy, plans and programs. Help influence and facilitate the cooperation of the three relevant governments and their citizens in the context of increasing economic trade and social links on a vitally important topic - the environment. Manage a large multi-national and leading edge technical staff.

Seasoned international executive...with extensive management experience and a demonstrable track record of dealing with complex international matters. Possess the ability to work with and facilitate agreement among international commissions, financial institutions, governmental and non-governmental organizations. Must have substantial knowledge of environmental matters including trade and environmental issues in North America. U.S. citizen fluent in English and either French or Spanish.

For a copy of the full Statement of Qualifications, please reply by sending your CV, quoting reference 3308/E and stating current salary to stacy.cook@boyden.com For more information, please call either Tim McNamara or Lance Wright in our Washington D.C. office on 202.331-3390.

Boyden

217 E. Redwood Street, Suite 1600, Baltimore, Maryland 21202-3316

Fax: 410.625-3801

www.boyden.com

To meet the growing demand for its services in
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Consultants and Managers

for long-term assignments in the following areas:

- **Management of Basket- and Trustfunds**
- **Private Sector Promotion (SME)**
- **Framework for privatisation and market economy**
- **International trade law (WTO accession, trade with EU)**
- **Rural Development**
- **Environmental Protection**
- **Water and Waste Management**
- **Development of the Health Sector/Aids**
- **Primary, Secondary and Technical Education**
- **Dezentralisation and Municipal Development**

Qualifications: University degree in areas related to the above and/or several years equivalent experience combined with relevant professional experience in the region required; Work experience with international donors (EU, World Bank, BID etc.) as well as proficiency in Spanish or Portuguese and English essential; Management skills a valuable asset.

GTZ (Deutsche Gesellschaft für Technische Zusammenarbeit) GmbH operates globally on behalf of the German Government as well as other governments and international donors, assisting and advising on the implementation of technical assistance projects in transition and developing countries.



Application: Please send a detailed resume quoting reference LAC to
GTZ International Services
Human Resources Unit
P.O. Box 5180, 65726 Eschborn, Germany
e-mail: DG-Team-5@gtz.de

<http://www.gtz.de>

Senior Equity Research Analyst UK Mining Sector

A major global bank is looking to strengthen its global mining equity research capabilities in its investment banking division, where it has historically enjoyed a prominent role. Members of the global team benefit from consistently strong flow of information from various research centres around the world and from leading metal trading operations in London and New York. The candidate will have the advantage of working alongside a powerful securities and research organisation with a highly ranked team in the mining sector.

The position:

This role offers exposure to fundamental company research and global company valuations, as well as the sale and marketing of the product on a worldwide basis. Sub-sector coverage includes:

- UK Diversified Mining Companies
- Global Diversified Mining Research
- Global Base Metals Research

Responsibilities:

- Financial analysis, modelling and research
- Sector responsibility
- Participation in client meetings, presentations and field trips
- Origination
- Involvement in the execution of transactions

Requirements:

- Financial analysis experience of major mining companies at a major Investment Bank; and
- Team-orientated player who appreciates deadlines and thrives under pressure

Candidate will be expected to display excellent analytical and communication skills. Previous exposure to and a clear interest in the sector are a prerequisite.

This position offers excellent prospects for career progression within one of the largest financial institutions in the world.

To apply, please contact:

Box 4121
The Economist
25 St. James's Street
London SW1A 1HG



Position:
EXECUTIVE DIRECTOR & CHIEF EXECUTIVE OFFICER

Organization:
**Qatar Foundation for Education, Science and
Community Development**

Location:
Doha, the State of Qatar

The Qatar Foundation (QF) seeks an Executive Director to be responsible for managing, planning and overseeing its educational, developmental and degree-granting programs. The Foundation is a private non-profit organization founded in 1995 to develop and implement educational, scientific research and community development.

The Foundation's current projects include the **Weill Cornell Medical School**, the **Virginia Commonwealth University School for Art & Design**, the **Qatar Academy (K-12)**, the **Learning Center** (for children with learning difficulties), the **Academic Bridge Program** (a university preparatory program), and the **Family Development Center** (an NGO for family empowerment). Plans are underway to establish degree-granting programs in Business Studies, Engineering, and Information Technology. Additional information is available at www.qf.edu.qa.

Responsibilities:

The Executive Director will be responsible for

- Managing the QF's overall operations in line with its vision, goals and Board of Directors directives;
- Assisting in defining and implementing the QF's long-term strategy and annual targets;
- Reviewing the annual business plans and budgets of the QF and its Centers;
- Ensuring the implementation of QF's policies and procedures;
- Recommending changes in operations, goals and strategies and implementing Board decisions;
- Promoting the QF's image in the community and internationally;
- Recommending new initiatives with which the vision of the QF will be asserted.

Qualifications:

An advanced degree in Business Administration, Education, Finance, Public Policy or other relevant discipline is preferred. Strong oral and written communication skills are required. The successful candidate will have proven skills in team leadership, project management, and strategic planning. He/she also will have demonstrated an understanding of trends in international education. Leading candidates will have extensive experience as a senior line administrator in educational, scientific, research or related organizations. Success as the chief executive officer of a university or other complex organization is an asset.

Contact Information:

Korn/Ferry International, which is assisting with this search, invites confidential inquiries, applications, and nominations. Nominations should include addresses, telephone numbers and e-mail addresses. Applications, including a current resume and letter explaining relevant experience, may be directed in total confidence to

John Kuhnle, Managing Director
Korn/Ferry International
900 19th St., NW; Suite 800
Washington, DC 20006
Fax: 202/318-4475

E-mail (preferred): anne.reich@kornferry.com



Nurturing Innovation, Enhancing Life

Strategically located within the heart of Asia, a dynamic and fast growing region, Singapore has established itself as one of the most competitive economies in the world. Consistently voted as amongst the best business destinations, it is supported by an increasingly globally competitive workforce. Committed to become Asia's biomedical sciences hub, the industry is being developed as the fourth pillar of the country's economy. Extensive resources are being invested in Singapore's industrial, intellectual and human capital, paving the way for partnerships with international biomedical sciences players. Together these companies play an integral role in the global biotech business, undertaking a wide range of activities from R&D to clinical research and manufacturing.

Founded in 2000 with investments from the biomedical sciences investments arm of the Singapore EDB and U.S. based Chiron Corporation, S*BIO is Singapore's first fully integrated drug discovery company. Our vision is to become a globally competitive and successful biopharmaceutical venture to discover and develop products stemming from our own leading edge research. Leveraging on Chiron's leading technologies, S*BIO is committed to drug discovery in an effort to become a recognized player in the international biotech space.

We are seeking a dynamic and high caliber executive to helm this dynamic and fast growing company.

Chief Executive Officer

The Position

Based in Singapore, the CEO will provide strategic leadership in mapping out a world-class business strategy that will further grow the business, and translate research results into valuable products with commercial biotech applications.

With a proven track record in developing a robust pipeline, he/she will build upon the company's research capabilities and sharpen its competitive advantage through an aggressive combination of in-house R&D, strategic partnerships with external groups and acquisitions. With sharp business acumen and financial savvy, the CEO will be the central figure leading the company's future capital formation efforts. Through a well conceptualized entrepreneurial strategy, the CEO will integrate the product development platform to deliver company and industry wide innovations.

The Person

- A dynamic business-building executive with a proven track record of between 12-15 years of demonstrated successes.
- Impeccable leadership and strong business management skills, preferably in the biomedical and/or pharmaceutical industries. Entrepreneurial company experience will be an asset, as is the experience in taking a company through Initial Public Offering (IPO).
- Experience in capital formation through private and/or public sources and the development of strategic partnering transactions of both a financial and scientific nature.

We are offering an internationally competitive remuneration package which includes an attractive base salary, bonus plans, stock options and executive benefits. Interested applicants should apply in strict confidence to the address below. For more information on S*BIO, please visit our website.

S*BIO Pte Ltd
The Human Resources Manager
1 Science Park Road, #05-09 The Capricorn,
Singapore Science Park II, Singapore 117528.
Email: execrecruit@sbio.com

Website: www.sbio.com

CHIEF EXECUTIVE

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The Board of Directors is seeking to appoint a Chief Executive following a sustained period of strong growth and international development.

The successful candidate will be able to demonstrate:

- Exceptional strategic leadership in a complex environment delivering challenging agendas
- Strong commercial acumen
- The credibility, experience, skills and presence to negotiate with and influence senior figures in education, business or government in the UK and internationally
- The ability to motivate a highly talented team
- Outstanding ambassadorial qualities

Further details, including information on how to apply, can be obtained from Barbara Stephens on 0207 317 4600 or downloaded from www.mba.org.uk. The closing date for applications is Friday 25th October 2002.

The Association of MBAs is committed to equal opportunities.



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INVESTOR IN PEOPLE



The Ford Foundation Representative (#192) India, Nepal and Sri Lanka

Based in New Delhi, the Representative directs the Foundation's activities in India, Nepal, and Sri Lanka, providing overall leadership to the Foundation's grant-making programs, managing the office, and representing the Foundation to various organizations and the public. Specifically, he/she assesses political, social, cultural, and economic developments in the region for their implications for the Foundation's programming; and supervises program staff in developing, monitoring, and evaluating grants and projects within the office's major fields of programmatic concern. Manages the office's grant and management budgets, monitors the office agreement with the Indian government, oversees legal matters, and supervises administrative staff. He/she maintains effective ties with local leaders, governmental agencies, NGOs, and other donors. Collaborates with other Foundation representatives in developing Asia-wide regional strategies and with program staff worldwide in shaping the Foundation's global work. He/she also manages own grants portfolio.

Qualifications: Demonstrated leadership, planning, management, and analytical skills; excellent written and oral communications skills in English; knowledge of the region's history and culture; in-depth understanding of development and social change processes; a relevant graduate degree. Also desirable are fluency in one or more South Asian languages; previous experience in India or the region; familiarity with the Foundation or philanthropy; and expertise in one or more of the Foundation's current program interests.

To apply send resume, substantive cover letter (indicating position #192), and brief writing sample (5-20 pages of original work) to:

Ms. S. Ashton at 320 East 43rd St, New York, NY 10017, USA,
or email (resumes@fordfound.org) preferably by December 15, 2002.

For more information on the Ford Foundation, visit www.fordfound.org.

The Ford Foundation is an EEO employer.



International Cocoa Organization

PROJECT OFFICER/ECONOMIST LANGUAGES/CONFERENCE OFFICER LIBRARIAN/IT OFFICER

The International Cocoa Organization (ICCO) seeks candidates for the posts of Project Officer/Economist, Languages/Conference Officer and Librarian/IT Officer. ICCO is an inter-governmental organization made up of 19 members from producing countries and 22 members from consuming countries.

PROJECT OFFICER/ECONOMIST

REQUIREMENTS

- Candidates shall possess an advanced university degree (Masters or equivalent), in Economics, including training in quantitative analysis and international trade.
- At least five years post qualification experience in project development/monitoring and preferably also experience in market research or empirical research connected with primary commodity markets, preferably in cocoa. A higher level degree (Ph.D or equivalent) may be substituted for two years' professional experience.
- Practical and analytical skills for project analysis and monitoring as well as the capability to perform economic studies on the cocoa sector.
- Fluency in English and a working knowledge of French.
- Experience in drafting analytical reports of publishable standard in English.
- Skilled in the use of computers for economic analyses.

TENURE: Five (5) years, with the possibility of extension.

DUTY STATION: Abidjan, Côte d'Ivoire.

REMUNERATION

The International Cocoa Organization offers a competitive, tax-free salary based on Grade P.2/3 of the United Nations salary scale in addition to other benefits, including Provident Fund, medical insurance, education grant and home leave travel. The net salary plus post adjustment presently ranges from US\$52,369 to US\$90,239 per annum.

LANGUAGES/CONFERENCE OFFICER

REQUIREMENTS

- Candidates shall possess a good university degree, preferably in modern languages, majoring in English and French. Working knowledge in Spanish and/or Russian desirable. Skill in drafting English texts is essential.
- Typing and computer skills; in particular, ability to use the Microsoft Professional Office Suite is required.
- A minimum of three years post-graduate experience as an interpreter/translator, precis-writer, journalist or similar background.

TENURE: Five (5) years, with the possibility of extension.

DUTY STATION: Abidjan, Côte d'Ivoire.

REMUNERATION

The International Cocoa Organization offers a competitive, tax-free salary based on Grade P.2/3 of the United Nations salary scale in addition to other benefits, including Provident Fund, medical insurance, education grant and home leave travel. The net salary plus post adjustment presently ranges from US\$52,369 to US\$90,239 per annum.

LIBRARIAN/IT OFFICER

REQUIREMENTS

- Candidates shall possess a good university degree in Information Technology/Library Studies with a minimum of two years' post-graduate experience in the development of databases.
- Excellent knowledge of the library environment and practices. A diploma in library science would be an advantage.
- Complete command of oral and written English; in addition, a knowledge of French and/or Spanish would be particularly useful.
- Knowledge of computer programmes, such as Windows, Microsoft Word and database programmes.
- Ability to use the Internet, HTML, and e-mail programmes is essential.

TENURE: Five (5) years, with the possibility of extension.

DUTY STATION: Abidjan, Côte d'Ivoire.

REMUNERATION

The International Cocoa Organization offers a competitive, tax-free salary based on Grade P.1/2 of the United Nations salary scale in addition to other benefits, including Provident Fund, medical insurance, education grant and home leave travel. The net salary plus post adjustment presently ranges from US\$41,692 to US\$71,926 per annum.

All applications shall be submitted in English and include a covering letter, curriculum vitae and recent photograph. The deadline for receipt of applications is **31 October 2002**. Applications are to be addressed to the Officer-in-Charge, International Cocoa Organization, 22 Berners Street, London W1P 3DB, United Kingdom, e-mail: head.admin@icco.org

Executive Focus

The United Nations Development Programme (UNDP) is the UN's global development network, advocating for change and connecting countries to knowledge, experience and resources to help people build a better life. We are on the ground in 166 countries, working with them on their own solutions to global and national development challenges. As they develop local capacity, they draw on the people of UNDP and our wide range of partners.



Senior Field Economists

The UNDP's Regional Bureau for Africa is seeking to employ four experienced professionals (three francophone and one anglophone) as Senior Field Economists to head Economic Units in Country Offices in Africa.

Under the direct supervision of the Resident Representative/Resident Coordinator, Senior Field Economists (SFE) are responsible for the following:

- Advise the programme country on issues related to sustainable human development contributing to the articulation of a long term national vision, and the formulation of strategies, policies and actions to attain it.
- Analyze the country's assets to identify constraints on development based on socio-political and economic trends and their impact on the people.
- Evaluate on-going macro-economic policies and their particular impact on poverty and the environment.
- Identify ways of strengthening national capacity, for negotiations and policy dialogue with the international community and development stakeholders including UN system partners.
- Strengthen the capacity of the Country Office by adopting, refining and ensuring complementary/integration of existing UNDP initiatives and the identification of new entry points for UNDP/RBA support.

Requirements:

- Post-graduate degree in Economics. Ph.D. desirable. Excellent oral and writing skills in French and/or English.
- Demonstrated mastery of macroeconomic aspects in the African region and at least ten years of increasingly responsible professional experience in the field of economic development.
- Strong managerial and communication skills. Experience in the development of strategic partnerships.

For further requirements and full job descriptions, qualified candidates are invited to visit UNDP's Website at www.undp.org/jobs (other current jobs) and submit applications by 7 October 2002 at the latest.

CV could also be submitted electronically to leena.dsouza@undp.org or by fax to UNDP Hqts. in New York: (212) 906-6478



United Nations Office for Project Services

The United Nations Office for Project Services, Executing Agency for the United Nations Development Programme Global Environment Facility Unit and the Government of Lesotho seeks qualified candidates for the position of:

CHIEF TECHNICAL ADVISOR

Conserving Mountain Biodiversity in Southern Lesotho (ref: LES/97/G31)

Based in Maseru, Lesotho the project seeks to ensure the conservation and sustainable utilisation of unique alpine and montane landscapes in Southern Lesotho through the creation of a network of small, protected areas and the improvement of resources management in areas outside protected zones. The overall project goal is to ensure the conservation and sustainable utilisation of unique alpine and montane landscapes in Lesotho.

Primary Responsibilities

Under the overall supervision of UNOPS, the local supervision of UNDP Lesotho and the National Environment Secretariat in the Ministry of Tourism, Culture and Environment (NES) the CTA shall be responsible for the following tasks:

- Be responsible through the Director NES, and the National Project Manager to the National Project Steering Committee for the timely provision of advice and support as to the efficient implementation of this project. In order to achieve this the CTA will ensure close liaison with the National Environment Secretariats and Project Management Team at both Central and District levels.
- Assist in the organisation of workshops, study-tours and fellowships, and ordering of project equipment.
- Assist in the preparation of TORs for consultancies and contracts within the project, advise and supervise such consultancies and contracts, as needed.
- In consultation with national project staff promote awareness of regional and cross-border conservation.
- In consultation with National Implementing Agencies, liaise with other organisations dealing with the conservation of Biodiversity in the region, including international and bilateral donor agencies, technical agencies and NGOs.
- Advise national and district agencies, as requested, on issues relating to Biodiversity in Lesotho and the region.
- In collaboration with NPM, prepare progress reports as needed by project management and supervisory agencies.
- Undertake other relevant duties as requested by the National Project Steering Committees.

Qualifications:

The CTA will have over 10 years professional experience in the conservation and management of tropical natural resources, or rural development activity. Proven experience with participatory management and capacity building at decentralised levels will be an essential pre-requisite. The CTA will be a person of international standing in these fields, with the capability of advising governments on people - Biodiversity interaction issues. The CTA will have considerable experience in project management, be able to work within a team approach and be familiar with field operations. Ideally the CTA will have extensive working knowledge of the African region and UN operations.

Application deadline: 8 October 2002

Estimated starting date: Immediately following selection (November 2002)

Contract Duration: 1-year full-time position (renewable for second year)

Remuneration: A competitive tax-free salary at P-4/P-5 level depending on experience and qualification

Interested applicants are invited to visit our website: www.unops.org for further details on this vacancy announcement, and to send a cover letter and curriculum vitae to **Katherin Topar-Michon, Division for Environmental Programmes, United Nations Office for Project Services, 405 Lexington Avenue, New York, NY 10174, USA** Fax: 212-457-4044. e-mail: katherintm@unops.org. Only applicants selected for interviews will be contacted.



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RAIL REGULATOR

SHAPING THE FUTURE

From its base in London, the Office of the Rail Regulator is playing a leading role in shaping the incentives for companies in an industry where better performance and significant growth are key public policy objectives. To meet new challenges, this independent body is strengthening its team by the appointment of three top economists.

Senior Economist – to £52,000

You will play a lead role in any future reviews of access charges, taking responsibility for the development of specific areas of policy. The emphasis is on sound regulatory economics and innovative approaches.

With at least four years' experience as a professional economist gained in a regulatory authority, regulated industry, or consultancy, your practical experience is likely to include work on a major periodic or price control review. You will need to be able to apply economic principles to a wide range of regulatory issues, including charging policy, the development of incentive frameworks and financial analysis. First class communication skills are a must, given the need to consult widely. Prior knowledge of the rail industry is desirable but not essential.

Senior Economists (two posts) – to £42,000

You will contribute to all aspects of ORR's work, and make a major contribution to any future reviews of access charges frequently taking the lead on individual projects.

You will have at least two to three years' practical experience as an economist in a commercial environment or with a regulator. Your key skills will include the ability to turn a complex mass of operational, economic and financial data into sound evaluations and policies. Your previous experience might include work on project appraisal, charging, expenditure assessments and/or financial modelling.

All three positions are permanent and the package, which includes excellent benefits, may be increased for exceptional candidates.

For an application pack please call Gill Atkinson or Bob Franklin on 020 7636 5444, or forward a CV outlining your suitability for the post to Chartwell Search & Selection Ltd, St George's House, 14-17 Wells St, London W1T 3PD – e-mail: gill@chartwellsearch.co.uk, to arrive by the closing date of 4th October 2002.

ORR is committed to equal opportunities. We welcome applications from candidates regardless of gender, ethnicity, disability, sexual orientation, religious belief or any other irrelevant factor.



CHARTWELL
SEARCH & SELECTION



INVESTOR IN PEOPLE

King Fahd University of Petroleum & Minerals Dhahran, Saudi Arabia

College of Industrial Management
Department of Finance and Economics

SAUDI ARAMCO CHAIR IN ENERGY ECONOMICS

The Department of Finance and Economics at the King Fahd University of Petroleum & Minerals invites applications and nominations for a newly established Saudi Aramco endowed Chair in Energy Economics.

The applicants for the Chair should have a distinguished background in teaching, research, and consulting since they will be occupying a Chair that will direct and guide the Department towards excellence in research, business consulting, and teaching in the fields that are related to Energy Economics subjects. In addition, he will be expected to:

- Conduct research of direct relevance to the energy sector and to energy economics in particular.
- Teach graduate and undergraduate courses in the areas of Economics in general and Energy Economics in particular.
- Create, develop, guide, and participate in short courses offered by the Department of Finance and Economics in collaboration with other faculty members.
- Offer technical and professional consulting assistance and services to both private and public firms in Saudi Arabia.
- Create and participate in programs with a special focus on energy economic trends that concern both Saudi Arabia and the rest of the world in collaboration with other faculty members.

Salary/Benefits: The compensation package will be competitive and commensurate with the position of this type. The package includes: a furnished centrally-air conditioned housing unit with essential utilities and maintenance; air ticket to Dammam on appointment and annual repatriation air tickets for up to four persons; local transportation allowance; fee assistance for school going dependent children; two months paid summer leave and end-of-service gratuity.

In addition to normal university benefits, the endowed Chair provides for secretarial support and other operational activities.

Letters of nomination, curriculum vitae, and names of three referees should be sent to:

Dean, Faculty and Personnel Affairs, KFUPM Box # 5005,
DEPT. SACEE-2002, Dhahran 31261, Saudi Arabia
Fax: + 966-3-860-2429 E-mail: faculty@kfupm.edu.sa
Website: <http://www.kfupm.edu.sa>

the world trade institute

Director of Legal Research

The World Trade Institute is seeking to appoint a new half time Director of Legal Research in International Trade Law. The current incumbent, Dr. Christine Breining, has recently been appointed to a senior academic position in the Faculty of Law at the University of Zurich.

The holder of this position shall direct the legal side of the WTI's research agenda. To date, the WTI's research program has focused on WTO decision-making and dispute settlement, intellectual property rights, financial services, and competition policy. The ideal candidate will be able to translate research findings into policy advice and, should the opportunity arise, externally-funded research projects. The Director of Legal Research may also undertake some teaching at the graduate level at the WTI (in the WTI's flagship program Masters in International Law and Economics -MILE, as well as in other programs), which will be remunerated separately. There will be limited additional teaching responsibilities at our founding universities, those of Berne, Fribourg, and Neuchâtel.

Applicants are expected to hold a Ph.D. in law with a specialization in the field of international trade law. The successful applicant has either an impressive research record or the clear potential to produce high quality research in international trade law and the legal analysis of international commerce, as well as a keen interest in linkages between the economic theories underpinning international trade and international economic law. Teaching experience and the ability to lead an interdisciplinary research team (law and economics) is expected. The applicant will be fluent in English and professionally conversant in either French or German. Some familiarity with the Swiss university system would be an advantage. The World Trade Institute is an equal opportunity employer. The contract is for a limited term and will terminate in December 2005.

Applications

Applications should be made exclusively via email at this stage and be received by November 10, 2002. Please address your application to Professor Thomas Cottier, Managing Director, World Trade Institute (thomas.cottier@iew.unibe.ch). Please send a cover letter outlining your research interests as well as a CV, which should include a list of your publications. The appointment of the successful applicant will be made by a select committee composed of the Directors and Board Members of the WTI and in consultation with leading members of our international faculty.

World Trade Institute, Hallerstrasse 6, 3012 Berne, Switzerland
Tel +41 31 631 32 70 Fax +41 31 631 3630
Email applications@worldtradeinstitute.ch
www.worldtradeinstitute.ch



United Nations Educational, Scientific and Cultural Organization

UNESCO is seeking qualified candidates
for the following post at its Headquarters in Paris, France

Director, Division for Freedom of Expression, Democracy and Peace (D-1) Communication and Information Sector

Main responsibilities

Under the authority of the Assistant Director-General for Communication and Information, you will be responsible for the formulation, execution and evaluation of UNESCO's programme on freedom of expression, democracy and peace. In particular, you will plan, manage, direct, implement and report on actions relating to:

- The promotion of freedom of expression, pluralism and independence of the media;
- Strengthening media in support of democracy and peace, especially in countries in transition, conflict or post-conflict areas;
- Provision of support to public authorities to bring their legislation and policies in line with recognized international standards of democratic media environment;
- The follow-up of the declarations and plans of action of regional seminars on the promotion of independent and pluralist media;
- Consolidation of alert networks aimed at providing more effective protection to journalists;
- Liaison with NGOs and other professional bodies working with UNESCO in the programme.

Qualifications and Experience

- Advanced university degree in communication, political or social science or international law.
- Extensive international experience (at least 10 years) in the field of the media and international relations.
- Recognized leadership in the field of press freedom, media pluralism and independence.
- Excellent command of written and spoken English or French, with excellent drafting ability in one of them, and a good command of the other language.

Terms and Conditions

Post is at D-1 level common to the United Nations system, with a salary composed of base salary and post adjustment, which at the present dollar exchange rate totals approximately US\$89,425 (without dependants) or US\$96,745 (with dependants) per annum, exempt from all direct taxation. In addition, an international benefits package is offered.

For more information on UNESCO's programmes, consult our website: <http://www.unesco.org/> and on the post: <http://www.unesco.org/per/index.html>

To apply, address a detailed curriculum vitae in English or French, indicating birth date, nationality and gender, attaching an identity photograph and copies of diplomas to:

UNESCO, Chief, Recruitment and Staffing Section,
Bureau of Human Resources Management,
7 place de Fontenay, 75352 Paris 07-SP, France,
before the closing date of:

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Outward bound

Do developing countries gain or lose when their brightest talents go abroad?

"THE people I have recruited, I have convinced personally. I have gone to their houses, met their families. They come here because they see this as a challenge." Edi Rama, the mayor of Tirana, capital of Albania, faces a familiar struggle for a boss these days, to get and keep good staff. But he is fighting for talent in a country where GDP per head is under \$4,000—less than a quarter that of neighbouring Greece, where some 500,000 Albanian emigrants now work.

Mr Rama is increasingly in direct competition with much richer countries, too. Canada and Australia, which pioneered "points" schemes to select would-be immigrants with skills, have been tilting these to take an even higher proportion of such people, and the United States has rapidly increased the supply of temporary visas for skilled workers.

Even governments that once strove to keep people out are encouraging the skilled to come in. Germany's recent immigration legislation includes a points system for skilled workers. Britain has rapidly expanded the availability of work permits for skilled migrants, and pushed down the required level of skill. And many countries are softening the rules that normally force

foreign students to go home as soon as they graduate. Australia decided last year to allow foreign students of information and communications technology to apply for permanent residence on the basis of their education alone.

Migrating, legally or illegally, is expensive. So a higher proportion of the well-educated can afford to emigrate than of the poor. In some regions, the discrepancy is staggering. A study by Lindsay Lowell and Allan Findlay for Britain's Department for International Development found that three-quarters of Africa's emigrants have higher (tertiary) education, and roughly half of Asia's and South America's. Of the 1m people from India living in the United States, more than three-quarters of those of working age have a bachelor's degree or better. About 30% of all highly educated Ghanaians and Sierra Leoneans live abroad.

America, the world's biggest skills-magnet, absorbs large proportions of the most educated people from neighbouring countries. A survey of new legal immigrants to America finds that about 21% of them have at least 17 years of education, implying some postgraduate study, compared with only 8% of native-born Ameri-

cans. Cumulatively, estimates Lindsay Lowell of the Pew Hispanic Centre, a think-tank, 12% of Mexico's population with higher education is in the United States, and 75% of Jamaica's. Such figures are all the more striking because, in poor countries, only about 5% of the young tend to be in higher education.

Not only are the skilled disproportionately likely to leave: it is often the best of the crop. Although about 3% of Indian doctors emigrated in the 1980s, the proportion for graduates of the All India Institute for Medical Sciences, the country's best medical school, was 56% in 1956-80 and 49% in the 1990s. In the case of Mexico, says Agustín Escobar of CIESAS Occidente, a research institute, 12% of the total labour force is in the United States—but 30% of Mexicans with PhDs are there.

Education abroad aggravates the exodus. America educates one-third of all foreign students and, not surprisingly, about half of all students who get PhDs in the United States are still there five years later. The proportion rises to over 60% for those with doctorates in physical sciences or mathematics. Students from India, China and Britain are especially likely to stay on when their studies are over. Some acquire temporary visas for the skilled: some 23% of holders of H1-B visas in February 2000 had previously held American student visas. Some find American spouses, a quicker and more certain route to legal immigration. And some simply overstay.

Poor countries are not the only ones affected by outward migration. Australia and Canada not only lose their own people to the United States. They also find, to ▶▶

► their irritation, that the most skilled immigrants use them as entrepot countries, acquiring citizenship and education before moving on to the largest and richest job market in the world.

For Canada, membership of the North American Free-Trade Area has opened the door for a stream of southbound migrants. "They did a quick one on us," complains Don DeVoretz of Simon Fraser University. For every three Canadians heading south, only one migrant moves north. Again, it is mainly professional people who go. For the past five years, Mr DeVoretz claims, between 15% and 40% of each year's graduating class has headed across the border. Once again, it is the stars who are most likely to leave.

Losing the best

Does it matter if clever people leave in such numbers? For the world as a whole, it makes sense for the cleverest to exercise their skills where they earn the greatest reward. But what holds for the world may not hold for individual countries that lose large swathes of their educated middle class.

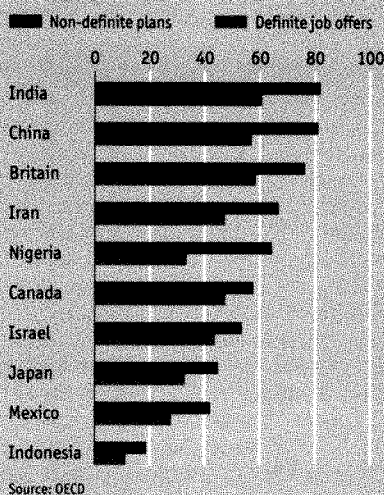
Some economists would argue that, overall, the impact of emigration on a sending country may be beneficial. Back in 1882, Knut Wicksell, a Swedish economist, argued that emigration would eventually rid his country of paupers, because poverty was an effect of excess labour and insufficient land. And the behaviour of wages in the main sending and receiving countries in the late 19th century suggests he may have been right. In Ireland, for example, though industrialisation was slow, the economic condition of Irish labourers rapidly improved as the migrants left, both in absolute terms and relative to those in Britain and the United States.

An exodus of the skilled may also raise pay for those left behind. In the mid-1990s, half the graduating physics class at Bucharest University left the country, says Ioan Mihailescu, the university's rector and co-author of a UNESCO study of the impact of the brain drain on the academic labour market in south-east Europe. Last year, that was down to 10%. The reason, he thinks, is that jobs for the highly skilled have grown as Romania's economy has expanded, and so have the wages of people with scientific and technological skills.

However, the loss of the skilled and educated may do more harm than emigration in general. These particular people create new jobs for others. Their departure removes the stabilising political influence of a middle class. And the exodus of scientists and academics wreaks particular havoc, especially if it happens quickly. Albania lost one-third of its qualified people in the decade after the fall of communism. The sheer speed of the exodus left no time for an orderly transition. Moreover, adds

America the magnet

% of foreign students who planned to stay in the United States after completion of their studies, 1997



Illir Gedeshi of the Centre for Economic and Social Studies, scientific research projects that take time to conduct fall apart when people leave because, as he puts it, "there is no inherited memory."

To the loss of productive potential, add the fiscal losses from migration. Taxpayers in developing countries have paid to educate many of those who leave (and who may well end up working in jobs below the level their qualifications would justify at home). And emigration leaves behind fewer workers to pay the cost of looking after the old. Although migrants boost the ranks of taxpayers in the countries they go to, they deplete them in their home country. A recent study of the fiscal effects of the Indian brain drain, by Mihir Desai of Harvard University and two colleagues, points out that the 1m Indians in the United States accounted for a mere 0.1% of India's population but earned the equivalent of a staggering 10% of India's national income. At home, of course, they would have earned far less. But they would still have been among the largest taxpayers.

How far does an outflow of skilled

workers bring a reward in the form of remittances? Overall, the sums that migrants send home to developing countries each year are astonishing: some \$60 billion through official channels and more—perhaps another \$15 billion—in various unreported ways. The inflow to developing countries doubled between 1989 and 2000. Officially reported remittances alone were about 20% more than official development aid over that period. And the gap is widening: official aid is dwindling, whereas remittances are still growing.

Remittances as stimulus

Until quite recently, development experts used to ignore these large flows, or worry that their impacts were mainly negative. Philip Martin of the University of California at Davis, who studied remittances to Turkey in the 1980s, found that they drove up the going rate for dowries, caused inflation of land prices and propped up an overvalued exchange rate. But even if they are spent on consumer goods, remittances may stimulate development, especially if they are spent locally. One study of Mexico suggests that each dollar of remittance generates three dollars of spending power.

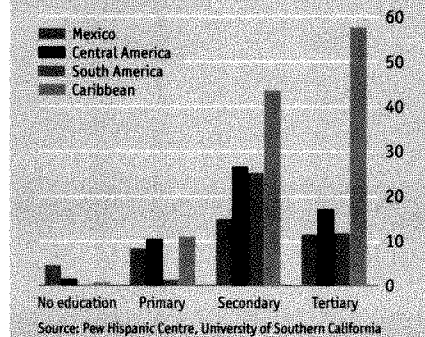
In general, though, remittance multipliers have the greatest impact in country districts, which tend to send the unskilled, not the skilled, abroad. And because the most educated are more likely to emigrate with their families and to integrate quickly into their new homeland, they seem less likely to send money back. One of the few attempts to estimate whether remittances by the skilled offset the loss of intellectual capital to the sending country concluded that they did not.

On the other hand, emigration may bring other benefits to the sending country. The possibility of leaving and the higher income to be earned abroad may encourage more people to go into higher education. As not everyone will leave, the result will be a bigger pool of skills than would otherwise be the case. In some countries, the education system is adapting to teach skills needed abroad: in Mexico, for example, the Monterrey Technological Institute has offered for two decades a curriculum and style of teaching designed to meet the demands of American multinationals. But, as Mr Escobar observes, these skills are also useful for their big Mexican competitors.

If those who go abroad subsequently return—a big "if"—they may import useful skills and contacts. And there are also signs that international trade flourishes between countries that export people and countries that import them. One Canadian study found that, during the 1980s, a 10% increase in the number of immigrants from a given country went with a 1% rise in exports to and a 3% increase in imports from that country. Increasingly, too, entre- ►►

Departing stars

% of educated people lost to the United States by sending region, 2000



preneurs from some Asian countries seem to travel back and forth. Of the 312 companies in the Hsinchu industrial park near Taipei, 113 have been started by American-educated Taiwanese engineers with professional experience in Silicon Valley, where 70 of the park's companies have offices to pick up new recruits and ideas.

Hanging on

What should developing countries do about the loss of skilled workers? Retention is the first line of defence. No country (North Korea and Cuba apart) now tries to stop its people from leaving. A few, such as China, lean heavily on the families of students studying abroad to ensure that they return. But most need to consider ways to make it more attractive to stay at home.

Top of the list should be making a country a good place to work. "I am always struck by how African leaders say they need the return of talent," says Mr Martin, "and yet my own students try every trick to stay, saying that they are in the wrong tribe, or do not have the right connections to get ahead." A culture where advancement depends on political affiliation rather than merit will lose bright people to societies where talent is what counts. This is particularly true in the public sector, including the universities, where professionals will stay only if professionalism counts. And countries need other attractions: Tirana's Mr Rama points out that his city did not even have a cinema until two years ago, and donors could not grasp why the lack of one was important.

Pay is vital too. But in order to compete for the brightest, poor countries need to pay them a much larger multiple of the average wage than would be true in the rich world. So global competition for this group will widen income disparities in developing countries. Again, that is a particular

problem in the public sector. George Soros's Open Society programme offers one modest solution: it tops up the pay of a small group of elite public-sector workers who have returned to countries in Central and Eastern Europe after being educated abroad. But even that brings problems: graduates who never went abroad to study resent the implication that their degree is worth less.

The way education is financed may have an effect on emigration. Mr DeVoretz calculates that the rate of return for a doctor who gets an education at a first-rate Canadian university and then goes to work in the United States is around 45% on the direct costs of his or her education. University education in Canada is heavily subsidised. If a would-be doctor had to pay the full cost of Canadian medical training, the return on a career south of the border would fall to 15%. Removing such subsidies, or replacing them with loans, would at least partly reduce the incentive to leave.

So, perhaps, might a tax on the diaspora. Jagdish Bhagwati, an economics professor at Columbia University, wants developing countries everywhere to extend their powers to tax their expatriates, in order to reclaim some of the value created abroad by highly skilled emigrants. But the omens are poor. Eritrea is a rare instance of a country that has, since 1993, imposed a tax of 2% of annual income on its expatriates. Apart from the sanction of social disapproval in the diaspora, those who do not pay find it hard to buy or keep land back home, or to get their passports renewed. The impost causes much friction.

But skilled people will continue to leave, and poor countries therefore need to devise ways to draw on their experience abroad. One way to encourage a sense of participating in two cultures, rather than one, is to extend the availability of dual

citizenship, something that developing countries have sometimes been reluctant to do. Another is to use the Internet to draw on expat skills and contacts. Jean-Baptiste Meyer, of the French Institute of Research for Development, has traced a growing number of virtual networks that link together a country's expatriate researchers, scientists, students or business folk. Some, such as the Global Korean Network or the Tunisian Scientific Consortium, organise annual conferences to discuss issues of interest to the members and the country of origin. Others undertake joint scientific projects.

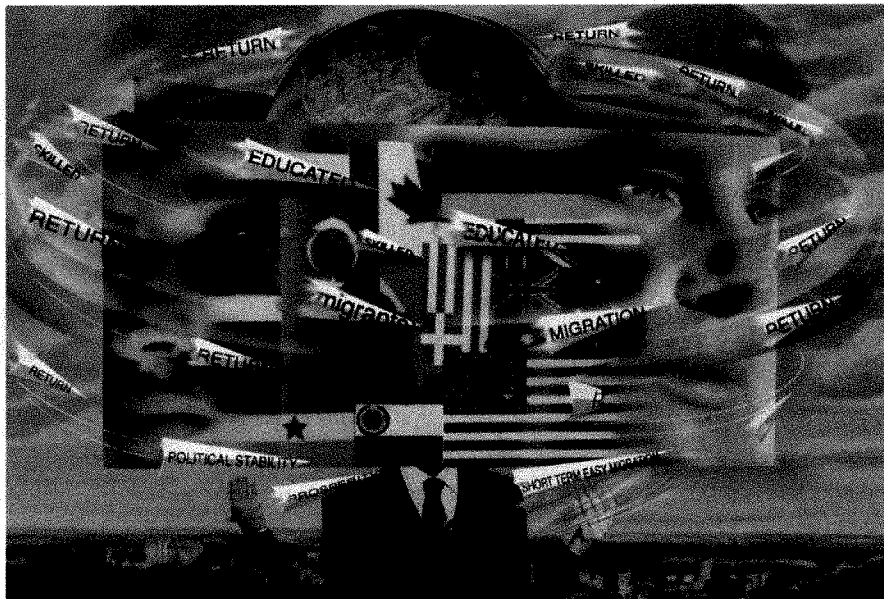
A two-way trade

A different approach is to bring back expatriates for short periods, with the guarantee that they will be able to return to their adopted country when their tour of duty is over. The United Nations Development Programme runs one such scheme, called Transfer of Knowledge Through Expatriate Nationals, or TOKTEN, helping skilled expatriates return to work on specific projects. The International Organisation for Migration runs a special project to bring back educated expatriate Afghans to help with rebuilding their country. So far, fewer than 300 have returned, but more than 4,000 have registered to do so.

What can the rich countries do? Already, some try not to recruit scarce health workers from poorer lands—although they cannot easily turn workers away who want to come. More usefully, they could put more money into tertiary education in poorer countries, aiming specifically to pay to train the people whom they are going to employ. One modest example: Bucharest university is talking to the Dutch government about teaching the language and other necessary skills to information-technology workers, teachers, nurses and police that the Dutch hope to recruit.

They should also make migration simple, but temporary. The tougher it is for migrants to enter a country, the more reluctant they will be to risk leaving to go home. However, the longer they stay abroad, the more likely their stay is to become permanent. The old contacts go, and it becomes harder to fit in. Mobility, which fits in comfortably with today's employment patterns, is more likely to benefit both sending and receiving countries than the old idea of migrating for good.

Once a developing country starts to grow rich, a return flow will build up of its own accord. Taiwan, South Korea and China all now receive considerable return migration. Ireland, once a land of emigrants, has become a country of net immigration. Given opportunities and political stability, good leadership and the rule of law, many of those who would otherwise leave a developing country will stay—and some of those who left will return. ■





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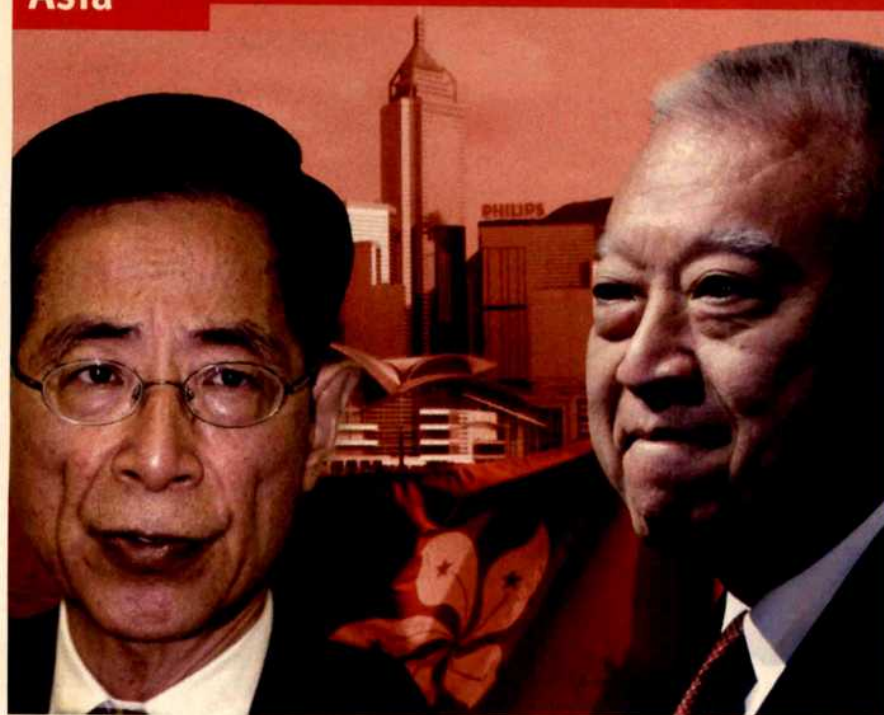
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Hong Kong

Death by slow boiling

HONG KONG

Are Hong Kong's liberties gradually being taken away?

THROW a frog into boiling water and it jumps out; gently bring it to the boil, and the frog, never noticing the incremental increases in heat, allows itself to be cooked. Is Hong Kong a frog in a pot in Beijing's kitchen? If so, then on September 24th the temperature rose another notch.

On that day, Hong Kong's government formally began—by circulating a consultation paper—the process of enacting a controversial set of laws against subversion, sedition, treason and other ills, as required by Article 23 of the Basic Law, the territory's constitution. Overdue and a mere matter of protocol, says the government—something that should have been seen to in 1997, when Hong Kong returned to Chinese sovereignty. An insidious threat to Hong Kong's liberties, counter the critics. If Article 23 could wait for five years, what's the urgency now?

To understand the controversy, it is necessary to know a bit about Article 23's history. The Basic Law came into being during the 1980s and 1990s, as a result of the negotiations between Britain and China about Hong Kong's handover. Its overarching formula came to be known as "one country, two systems". Hong Kong, in other words, would remain autonomous, and would enjoy freedoms absent on the Communist mainland. A principal conces-

sion to Beijing was a phrase, included in 1988, requiring Hong Kong to prohibit any act "to subvert" the central government.

The problem, however, was that subversion is an alien term to Anglo-Saxon common law, on which Hong Kong's legal system is based. After all, most citizens in free societies regard it as a basic right to subvert—peacefully—their own governments: they call it opposition. So a second draft, in February 1989, replaced "subversion" with "treason, secession, sedition or theft of state secrets", concepts already defined, if not much invoked.

Then came the Tiananmen Square massacre in June 1989. Hong Kong was horrified at the crimes committed by its future leaders, but the leaders were horrified in turn by the prospect that they might soon have to contend with similar uprisings in Hong Kong, where they would be powerless to crack down. The colony was rocked by huge demonstrations in support of the students. Supplies, money and, perhaps most important, newspapers were sent to them. In the months after the massacre, China insisted on a new draft. The final version of Article 23, in April 1990, restored the requirement for the prohibition of subversion, and added new ones aimed at links between "political bodies" in Hong Kong and abroad.

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31 Refugees from Malaysia

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"Isn't it obvious that, after Tiananmen, Beijing felt threatened and wanted more control?" asks Martin Lee, who helped draft the early versions of the Basic Law and now leads Hong Kong's Democratic Party, the closest thing to an opposition in Hong Kong's toothless and mostly unelected legislature. The fear is that the proposed laws are really targeted at groups such as Falun Gong, a spiritual movement considered an "evil cult" on the mainland but currently legal in Hong Kong. Tung Chee-hwa, Hong Kong's chief executive (pictured above right with Mr Lee), certainly appears to hate having to tolerate Falun Gong in Hong Kong. He might welcome means to brand the group as subversive and deal with it accordingly.

Falun Gong, moreover, is only the most obvious potential target of the new laws. Other dissidents are worried too. So are some journalists and academics, who fret about the clauses regarding theft of state secrets and sedition. Could a research paper on, say, Taiwan-mainland relations constitute a "seditious publication"?

The government, naturally, is working hard to allay these concerns. Not only, it says, has it compared its proposals to existing laws in countries far and wide, it has also complied strictly with international covenants on civil rights in the drafting. Besides, it adds, the point of the whole exercise is only to protect national security, not to limit anybody's freedom of expression. The definitions are tight enough, the government says, that most journalists and dissidents should have nothing to fear.

Ask, for instance, Elsie Leung, Hong Kong's justice secretary, about Falun Gong. She pulls a tome off her shelf and leafs through it to find some fine print that de- ➤

finds political bodies as organisations that "promote or prepare candidates for elections", under which definition Falun Gong is not a political body in Hong Kong, at least for the present. Or ask Regina Ip, the secretary for security, whether, under the proposed laws, she could extend the mainland ban of Falun Gong to Hong Kong. No, she replies, as Beijing at present does not ban the group on national-security grounds (required for a Hong Kong ban under the new rules) but under a different category, one for "evil cults". This is meant to be reassuring.

Critics fear this is all part of a pattern, whereby Mr Tung is slowly eroding Hong Kong's checks and balances. In July, he altered Hong Kong's colonial government structure, in which he sat atop an apolitical civil service. He replaced it with one in which he oversees a cabinet of ministers accountable only to himself, who is in turn accountable only to Beijing. It is these ministers who are now drafting Hong Kong's new laws. Every few months, it seems, the water gets a little hotter. ■

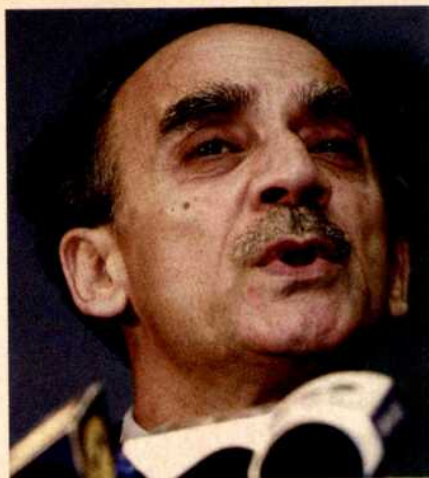
India

Junked

DELHI

Shame of the downgraded rupee debt

NO COUNTRY likes to be reduced to the status of a junk bond, so it is not surprising that a particularly proud and basically stable nation such as India was scornful when Standard & Poor's, a rating agency, downgraded rupee-denominated government debt on September 19th from BBB- to BB+. But India's loss of investment-grade status, and ranking with the likes of Costa Rica and Peru, had little impact on the markets. That was partly because the downgrade was seen as over-harsh when there has been no sudden change in economic fundamentals, and partly because 98% of the government's debt is in domestic markets. S&P cited the government's



Shourie snookered

"growing rupee debt burden" and its "inability to staunch the financial weakening of the public sector". Finance ministry officials replied that India's fiscal deficit had been stable for four years (though it is uncomfortably high at around 11% of GDP, taking central and state budgets together), and that reserves were a record \$62 billion.

But S&P did have a point about the public sector. The government has just postponed for three months the sale of its controlling stakes in two refinery and petrol-station companies, BPCL and HPCL. That decision encouraged political opponents of other imminent sales of shipping, aluminium and fertiliser companies to come out of the woodwork, and it now looks as if the government's most active reform initiative may have been halted. Having been ambushed on these sales by his cabinet colleagues, Arun Shourie, the reformist disinvestment minister, shows no signs at present of pursuing plans for privatising these and other corporations.

Adding to the gloom, the government had decided earlier last week to delay a decision on recommendations made by a planning group that foreign direct investment (FDI) restrictions in telecommunications, aviation and insurance should be relaxed. Atal Behari Vajpayee, the prime minister, had hoped to push through these changes to offset the impact of the privatisation delay. He might try again at a cabinet meeting due on September 28th.

FDI inflows touched a record \$1.35 billion in the first quarter of this year, boosted by several big items such as the \$200m purchase by Suzuki, a Japanese motor manufacturer, of the government's stake in its Maruti car joint-venture. The delayed privatisations would have triggered more such foreign purchases. But India's already shaky reputation as a reliable destination for FDI looks like receiving a further knock from a dispute, which the government is allowing to escalate, between BG (British Gas) and the public-sector Oil & Natural Gas Corporation over operating rights in a ▶▶

China

Enlisting gamblers

BEIJING

A cunning way to trap tax-dodgers

BAD times may be looming for Beijing's tax-dodgers. The city's government is introducing a scheme that it hopes will add more than \$100m to tax revenues next year by forcing businesses to issue proper receipts. The project involves turning receipts into scratch tickets that offer cash prizes and give consumers an incentive to make sure they are not given counterfeits.

Taiwan has successfully used a variant of this tactic for many years. Now China, faced with a fast-expanding budget deficit, is trying to harness public enthusiasm for lotteries to boost its revenues. Last year, the new system was

given a trial run in the capital's satellite town of Huairou. During the year, the town gave out \$17,100 in prize money and gained \$732,000 in additional tax revenue—a nifty return. From next week, the system will be promoted throughout Beijing's hotels, restaurants and other service establishments.

The new receipts have an "award area" which customers can scratch to reveal either the disappointing word "thanks" or a prize ranging from 100 yuan (\$12) to 5,000 yuan (\$605). To discourage forgeries, scratching another box reveals a code number. This can be entered, together with the receipt number, on a web page maintained by the Beijing Local Taxation Bureau.

But Beijing's vendors of fake receipts appear to be doing business much as usual. Outside Xizhimen subway station—one of their favourite haunts—peddlers call out "receipts, receipts" to passers-by. They are still selling old-style ones, which are eagerly bought by businesses and individuals hoping to defraud the taxman or their employers.

One man offers fake receipts for all of Beijing's top hotels at 50 yuan (\$6.05) apiece—less, if buying in bulk. Another peddler scoffs at the new system. When people need counterfeits of the new receipts, "We will definitely have them," she says. "We are the best."



► successful offshore oil and gas field.

Since the privatisation push began at the beginning of 2000, the control of 12 industrial and service companies has been sold (along with a clutch of hotels) to what are called strategic partners such as Suzuki, bringing 113 billion rupees (\$2.3 billion) to the government. Sensing increased market value as potential bidders lined up for future sales, the price of minority government stakes in 32 public-sector businesses listed on the stockmarket rose by more than 70% in the first five months of this year, when the sales momentum was picking up, and then fell back 20% after the negative BPCL and HPCL decisions. Pradip Bajaj, the official in charge of disinvestment, says that this shows the benefit of selling controlling stakes to strategic partners, who are willing to bid high prices.

Some critics prefer India's previous practice of floating public sector shares on to the stockmarket because this can delay change and does not pose such an immediate threat to vested interests. That view might prevail. With nine state assembly elections due in the coming year or so, and a general election in 2004, it seems unlikely that the government will be able to do anything very adventurous. ■

Gujarat

Waiting for the big one

DELHI

Another atrocity in Gujarat leaves India fearful

IN AN impressive example of what the Indian authorities can achieve when they are determined to prevent riots, the army was staging "flag marches" across the state of Gujarat as *The Economist* went to press. Police and paramilitary security forces were on patrol in major cities and towns throughout the country. All were trying, apparently successfully, to prevent a fresh round of religious violence, after a terrorist siege at a Hindu temple left 30 people dead, and the country's main Hindu fundamentalist group called for a nationwide strike in protest on September 26th.

The siege started late on the afternoon of September 24th when gunmen entered the Akshardham temple complex at Gandhinagar, throwing grenades and firing on worshippers. Some 500 people were rescued from the sprawling complex. The siege ended in the early hours of the following morning, when security forces killed the gunmen.

Gandhinagar is the seat of Gujarat's government, which was condemned earlier this year for standing aside during



Firefighters

Hindu-Muslim riots, in which more than 2,000 people are believed to have been killed. Those riots started when 58 Hindu pilgrims were burned alive on a train at the Gujarati town of Godhra. Hindus responded by going on the rampage.

No group has claimed responsibility for the latest attack. But L.K. Advani, India's deputy prime minister, and Narendra Modi, the state's chief minister and a prominent member of the ruling BJP party, both blamed Pakistan—an accusation quickly denied in Islamabad. Letters found on the bodies of a gunman were said to carry the title *Tehreek-e-Qassas*, an unknown group which Indian officials said could be linked to the Pakistan-based *Lashkar-e-Taiba*, allegedly involved in an attack on the Indian parliament in New Delhi last December.

Other Indian ministers were more cautious (though blaming Pakistan probably helped reduce the risk of a backlash against the Muslim minority by suggesting that the attack was inspired by politics, not religion). The siege coincided with elections in India's disputed territory of Kashmir which have drawn unexpectedly large turnouts of 40-50% in the first two rounds of voting. Referring indirectly to Pakistan, India's prime minister, Mr Atal Behari Vajpayee said the siege had been staged because opponents of the elections were "jealous" of their success.

Gujarat has been a potential tinderbox since the earlier riots. Mr Modi, one of the country's most controversial politicians, has recently been condemned for making inflammatory remarks against Muslims. He called the relief camps to which they fled during the riots "baby producing centres". That was a reference to a view held by hardliners that Muslims have large families in order to increase their religion's population in India.

Elections are due in Gujarat by the end of the year and the state is fearful of another outbreak of violence. The BJP has been trying to rein in Mr Modi, lest his extreme views costs them more votes than they win. Politicians such as Mr Advani and Mr Vajpayee, who quickly flew to the scene of the siege, made it clear to him that the attack was not to be used as an excuse for a second round of attacks on Muslims. "This game of violence and counter-violence has to stop," Mr Vajpayee said bluntly. Easier said than done. ■

Refugees from Malaysia

Island of fear

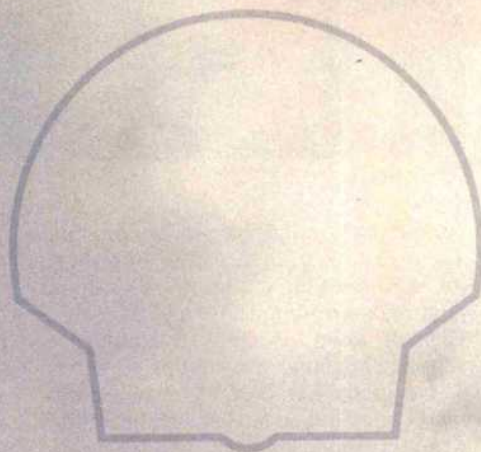
NUNUKAN

Thousands of "illegal" workers flee from Sabah

THE tiny Indonesian island of Nunukan has become a cramped refuge for thousands of Indonesians fleeing from Malaysia, where the government says any caught without work permits face jail and a caning. The government acknowledges that at least 12,000 have arrived, and more come every day. Add the workers' dependants and the number of refugees nearly doubles. Since the influx began last month, at least 70 have died, mostly from preventable diseases according to Post Seven, a Catholic relief agency.

After protests by Indonesia and other countries, Malaysia now says it has suspended its drive against "illegals". It does not care for its flag to be burnt publicly, as it has been in Jakarta. Those who have left Malaysia can return, it says, providing their passports are in order. But the dam- ►►

CLOUD THE ISSUE



PROFITS & PRINCIPLES.

The issue of global warming
has given rise to heated debate.
Is the burning of fossil fuels
and increased concentration of
carbon dioxide in the air a serious
threat or just a lot of hot air?

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age has been done.

It looks as though Malaysia, perhaps over-worried that among the Indonesians were members of the dreaded al-Qaeda, has badly misjudged the effects of its policy. Most of the Indonesians fleeing to Nunukan worked in Malaysia's eastern state of Sabah. Some have spent most of their lives there. Although the refugees include mechanics and maids, the largest number by far are plantation workers, mainly employed by Chinese Malaysians growing coffee, cocoa or coconuts. Their lack of passports and work permits has been tolerated. Some desperate employers have now sent them money to return to Sabah. Illegal labour has always been cheap, and can easily be disciplined with threats to report rebellious spirits to the police.

Despite the inconvenience of having thousands of unexpected guests camping in their backyards, the people of Nunukan are quietly benefiting from the influx. They charge those camping nearby for the use of their bathrooms. The Indonesian government has sent in teams of builders to put up huts for officials trying to sort out the mess, all of which means a bit more cash.

Nunukan has long been a base for cheap labour for Sabah, and the 20 or so firms in the business are dealing with applications for passports and work permits. Haji Ramli is one of the biggest operators. He used to be in the people-smuggling business but now, he says, he sends his clients to Malaysia the legal way.

Indonesia is providing free travel to Sulawesi or the other eastern islands the refugees mostly come from. Many have little enthusiasm for returning to Sabah. According to some plantation workers, life is close to slavery, with poor accommodation, a ten-hour working day, and pay the equivalent of about \$3 a day. If they have passports, the boss generally takes charge of them. They have three days off a year, Malaysian public holidays.

But, grim as this sounds, it is work. The alternative prospect in Indonesia is joining the country's 40m unemployed. ■

Demobilisation in Cambodia

Cam-bodge

KOMPONG CHHNANG

Turning swords into ploughshares is proving tricky

WHEN Pieng Iour joined the army in 1981, Cambodia was already a decade into its 30-year civil war. By the time he was demobilised last year, the endless fighting had not only left the country one of the poorest in Asia, but had also saddled it with an expensive and, in these peaceful days, over-large army. Yet Mr Pieng was able to step down only thanks to a \$42m demobilisation scheme paid for by the World Bank and other foreign donors, which aims to equip some 30,000 soldiers whose fighting days are over with the means to earn a living as civilians. Mr Pieng used a \$240 grant provided by the scheme to buy half a hectare (1.25 acres) of land on which he has planted rice. A free package of simple tools allowed him to set up house and start working the ground, while handouts of rice kept his family fed until his first harvest. When a promised sewing machine arrives, his wife and daughter hope to supplement the family's income as seamstresses. For a modest investment, his family has been transformed from a burden to the state into contributors to a recovering economy.

But Mr Pieng's neighbour, Ngem Sovantha, also an ex-soldier, has problems. Having spent his \$240 on medical bills, he borrowed from a loan-shark to buy a motorbike he uses to ferry his fellow villagers around for a fee. He is due to receive another motorbike under the demobilisation scheme, which he will sell, doubtless at a hefty discount, to pay off his debts. Why,

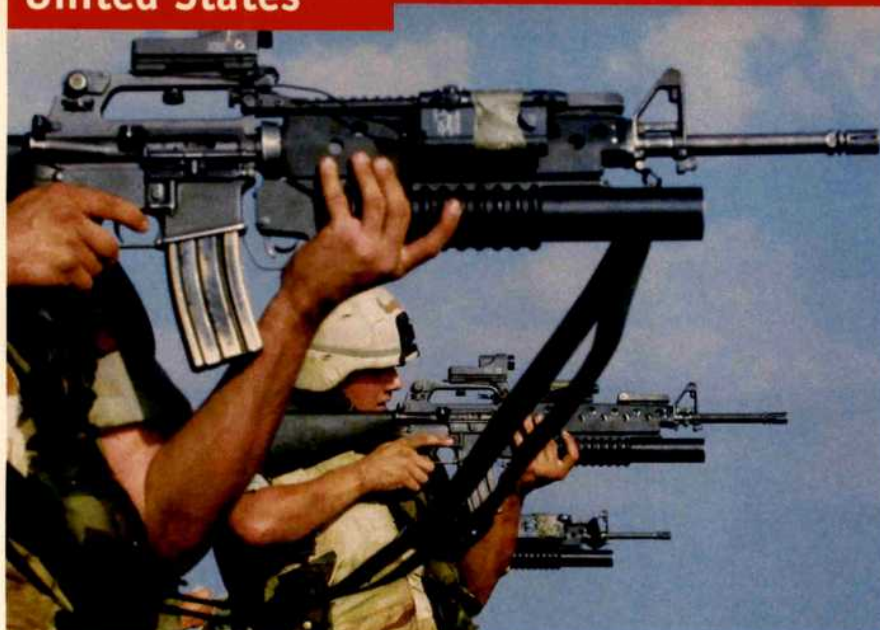
he wonders, could he not have been given its value in money instead?

The World Bank says that it limited the size of cash handouts for fear that officials would steal them or recipients squander them. Nor will it provide two things most ex-soldiers want: land (too many legal disputes) and cows (tricky logistically). Instead, on top of their \$240 grants, ex-soldiers can choose one of a range of items, such as a sewing machine, a motorbike or a generator. Like Mr Ngem, many plan to sell these straight away, and spend the proceeds on whatever they really need. That will allow a few local dealers to make a killing from the World Bank's caution. Those who keep their equipment might fare worse: many of the 50 demobilised soldiers in Mr Pieng's district plan to set up tailoring or taxi businesses as soon as their sewing machines or motorbikes arrive. The result of competing businesses, presumably, will be penury all round.

The government seems interested in military reform only as an excuse to prise money from donors. It has not provided details of what extra pensions or benefits the demobilised soldiers might receive, making it impossible to tell whether the programme is generous enough. So far only 15,000 of the nominally 120,000-strong military have been demobilised, all of them old or disabled or both. There are no clear rules about how the remaining 15,000 to be demobbed will be chosen, raising fears that they may have to buy their way on to the list. However the process works, it will leave the army top-heavy, with some 500 generals alone, and short on enlisted men. Because of this, the government periodically threatens to raise more recruits, rendering the exercise pointless. But whenever donors raise objections, as the World Bank did recently, Hun Sen, Cambodia's prime minister, threatens to call off the programme altogether. ■



Waiting for civvy street, and maybe a sewing machine



Foreign policy

Unprecedented power, colliding ambitions

WASHINGTON, DC

America's new National Security Strategy is radical, but not in the ways its critics tend to claim

GEORGE BUSH'S "National Security Strategy", released on September 20th, expounds no new ideas and does not change the focus of America's foreign policy. Nevertheless, it may be one of the most important geopolitical documents produced for a long time. Many people, inside and outside America, have puzzled over the administration's view of the world. They need not do so. The document puts it as clearly as anyone could wish.

It is bracingly blunt, as befits something written, in Mr Bush's words, so "the boys in Lubbock" can read it. Sentence one: "The United States possesses unprecedented—and unequalled—strength and influence in the world." Might globalisation restrict that power a little? No. The word "globalisation" does not appear. For Mr Bush, American power is what matters. Europeans need to grasp this.

There is no question of softening that power or letting it erode. ("Our forces will be strong enough to dissuade potential adversaries from surpassing or equalling the power of the United States.") The only question is what that power is used for.

The document spends most of its time on old and recent concerns: free trade, development, even AIDS. (Republicans used to argue that AIDS was not a security issue. No longer.) In some respects, the document has reassuring continuities with President Clinton's world view, though the Bush White House would hate any

such comparison. The strategy puts forward no new foreign-policy ideology. It is driven by changing circumstances, notably the Soviet collapse and America's resulting pre-eminence.

Early on, the document draws two clear lessons from the end of the cold war. One, "America is now threatened less by conquering states than we are by failing ones." Two, cold-war doctrines of deterrence and containment no longer work effectively in a world of "shadowy" terrorist networks. And since this is so, "to forestall or prevent...hostile acts...the United States will, if necessary, act pre-emptively."

Pre-emption is not new. America has acted pre-emptively before, notably in Central America. And though it now becomes a core part of foreign policy, it sits uneasily beside the statement that "our military must deter threats against us interests, allies and friends." Deterrence, clearly, is not dead.

A second tension is between the aims of defeating terror and promoting democracy. The document says that America aims to create "a balance of power that favours freedom" and claims that "the world's great powers find ourselves on the same side—united by common dangers." It moves to and fro as if these things were the same. They are not.

The first is about promoting values, the second about promoting order. It is simply not true that at the level of government all

the world's powers are on the same side in promoting democracy. And some of the steps you might take to defeat threats (co-sying up to Saudi Arabia, for instance) conflict with the aim of promoting freedom.

In that respect, argues Ivo Daalder of the Brookings Institution, the document is a faithful reflection of the different strands in the administration: the democracy-promoting "imperialists" such as Paul Wolfowitz, the deputy secretary of defence, who want to change the world; the "offensive realists", like Donald Rumsfeld, who want to use American power to prevent threats; and the "defensive realists" like Colin Powell, who still see a role for deterrence and for alliances with other countries.

But perhaps the most important influence is that of Condoleezza Rice, the national security adviser. Ms Rice is often regarded as a go-between in the Bush administration's internal wars. There is no discernible Rice world view, as there is a Powell or Rumsfeld one. Yet one may be emerging. The strategy talks a lot about "building good relations among the great powers"—the theme of an article she wrote in *Foreign Affairs* in 2000 (before Mr Bush's election). This is classic *Realpolitik*. The intriguing change now, however, is that these realistic means are being harnessed to more idealistic ends: "The United States must defend liberty and justice because these principles are right and true for all people everywhere."

If this is so, the tension between promoting democracy and defeating threats will be resolved in favour of promoting democracy. As the document insists, this will be by peaceful means wherever possible, with force used only as a last resort. But the new strategy will nevertheless set America on a course of encouraging change not only in Iraq but in Iran, Saudi Arabia and elsewhere. Let authoritarians take note. ■

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Re-enter Al Gore

To little effect

WASHINGTON, DC

The ex-vice-president hasn't stirred up anti-war feeling

THE most striking feature of America's debate about Iraq is that there isn't one. While Europeans march and yell, America's momentum towards war gathers pace without serious political scrutiny. Might that be changing? Don't bet on it.

For much of the summer, leading Democrats loudly proclaimed that they really, really wanted a debate. They were kidding. They wanted to get back to "kitchen-table" issues. Evidence for this is that as soon as George Bush asked for a congressional resolution backing war, Democratic leaders fell over themselves to sign up.

But now they do have a debate on their hands—courtesy of their former standard-bearer, Al Gore. In a speech in San Francisco on September 23rd, Mr Gore became the most senior politician so far to question the case for war.

He made four points. One, an invasion of Iraq would distract attention from destroying al-Qaeda. Two, by demanding a congressional resolution "in this high political season", President Bush is politicising the issue. Three, invoking a doctrine of pre-emption is unnecessary in Iraq and bad (because destabilising) elsewhere. Four, by squandering the international sympathy America attracted after September 11th last year, Mr Bush has undermined the coalition against terrorism.

None of these points is new. Brent Scowcroft, national security adviser to George Bush senior, has made the first and the last. Tom Daschle, the leader of the Senate, has accused the president of playing politics. Mr Gore's third point, about pre-emption, has not, however, been debated properly (see previous story).

But some assertions are dubious, such as the claim that "the vast majority of those who sponsored, planned and implemented [the September 11th attacks] are still at large." (Didn't the implementers kill themselves?) And some are worse than that, such as Mr Gore's claim that he "felt betrayed by the first Bush administration's hasty departure from the battlefield" in 1991. (In the Senate that year, he had said "I want to state this clearly, President Bush should not be blamed for Saddam Hussein's survival.")

Still, by virtue of having won the popular vote in 2000, and of having backed war against Iraq in 1991 (unlike most other leading Democrats), Mr Gore carries weight. His speech deserves attention. Whether it will get it is another matter.



He felt betrayed, he says

Though you would hardly know it from the consensus at the top, a majority of Americans oppose war in Iraq if it were carried out unilaterally. In this week's Gallup poll, only 38% of respondents said they would support American military action in Iraq if undertaken alone; only 37% would support it without congressional support. So you might think that Mr Gore's reservations would strike a chord.

But support jumps to 79% if American action gets United Nations support, or if other countries join in. Most polls put American support for a war in general (ie, without specifying conditions) at two-thirds. That is extremely high. According to Karlyn Bowman, a poll-watcher at the American Enterprise Institute, polls have never previously shown majority support for a war before it began. Moreover, Americans not only support war, they expect it. That is the most plausible explanation for the sudden jump in the number of those who now call Iraq the most important issue facing the nation, displacing the economy for the first time.

Mostly for that reason, Democratic leaders are likely to ignore both Mr Gore and the rearguard action he has encouraged among a few congressmen. Democrats may try to tone down Mr Bush's proposed (and sweeping) congressional resolution, which would authorise "all means he determines to be appropriate, including force, in order to enforce [UN resolutions], defend the national security interests of the United States against the threat posed by Iraq, and restore international peace and security in the region." But pass it they will. And then hope to move on to domestic matters. ■

America and Germany

The poisoned relationship

WASHINGTON, DC

And one that will be hard to detoxify

FOR the past few years, Washington's Embassyland has been the site of a war of bricks and mortar. A dozen countries have built embassies the size of palaces in a desperate attempt to outshine their rivals. This building war is a physical expression of a fundamental reality: that there is nothing more important in foreign affairs these days than currying favour with the world's only superpower. Over the past few weeks the German chancellor, Gerhard Schröder, has taken a different tack. As Washington sees it, he has in effect demolished the German embassy and replaced it with a huge neon sign saying "Go to hell, Yankee imperialists."

The White House simmered in silence while Mr Schröder made opposition to America's Iraq policy (even if sanctioned by the UN) a centrepiece of his re-election campaign. But when his justice minister, Herta Däubler-Gmelin, was reported to have accused George Bush of behaving like Hitler, focusing on a foreign foe to distract attention from his country's domestic woes (a fine example of the pot calling the kettle black), the White House went on the offensive. Both Condoleezza Rice, the national security adviser, and Donald Rumsfeld, the defence secretary, said American-German relations had been "poisoned".

Mr Schröder is now trying to mend fences. He has sent a personal letter to Mr Bush explaining the remarks of Ms Däubler-Gmelin, who has said that she will not serve in Germany's new administration. But so far the Bush administration is in no mood to kiss and make up. Ari Fleischer, the president's press secretary, complained that Mr Schröder's letter was not an apology (as it was not, since the chancellor did not believe his justice minister had said such a thing). Mr Rumsfeld pointedly snubbed his German counterpart, Peter Strüch, at this week's meeting of NATO defence ministers in Poland. (Scheduling problems, said he.) The White House makes it clear in private that it blames Mr Schröder for creating an atmosphere in which crude anti-Americanism has flourished. And there is a real worry that, just as NATO is trying to get an instant-response force set up, Germany will not be willing to play along.

How much longer will the poison last? Germany has already made one substantial attempt at detoxification, promising to take over (in combination with the Dutch) the burden of peacekeeping in Afghani- ▶

stan. The United States clearly needs Germany's support in rolling up terrorist networks, some of which have flourished among the country's Muslim population. Germany's security services have been some of the most assiduous in monitoring Saddam Hussein's weapons programmes. Most Germans are not wildly anti-American, nor forgetful of America's help against Soviet expansionism. They just have a visceral dislike of "cowboyism", and think Mr Bush's Iraq policy is a case of it.

But Mr Bush is not a man who is inclined to forgive and forget. He sees politics in highly personal terms: hence his enthusiasm for looking into Vladimir Putin's soul and for inviting world leaders to his ranch in Crawford. He is capable of nursing grudges for years: witness his refusal to invite John McCain to the signing of the McCain-Feingold legislation overhauling campaign finance, perhaps the most important legislative achievement of Mr McCain's career. The new German government will have to work hard if it wants to be friends again. ■

The Democrats

We're different. Oops

WASHINGTON, DC

Trying to switch the election debate to domestic policy may well not work

THE Democrats are desperate to change the subject of November's mid-term elections from Iraq to the domestic issues on which voters favour their party by large margins (see chart). The problem is that they may have cause to worry about their home-front ideas, too.

The Senate majority leader, Tom Daschle, gave a speech last week about long-term unemployment (now 1.5m people), dwindling retirement accounts, rising health-insurance costs and thousands of foreclosed mortgages. This leading Democrat blamed the gloomy scene on tax cuts and the return to budget deficits that will hamper government investment in "na-

tional defence, education and health".

But Mr Daschle could offer no coherent way to fix fiscal policy. He stopped short of proposing to rescind or postpone the tax cuts. No wonder: opinion polls show that most Americans want to keep the cuts, and 12 of his Senate colleagues (five of whom are now embroiled in fierce re-election battles) voted for them in 2001. Mr Daschle has similar trouble attacking the budget deficit, because he wants to spend at least \$9 billion more than the president in the fiscal year starting on October 1st, which would become \$200 billion over the next ten years.

The politics of the budget process further weakens the Democrats' position. Because Congress is so far behind on the 13 bills that will finance the government after September 30th, Congress will surely have to send the president a stop-gap measure to provide temporary money at last year's level. The Democrats will have to accept Mr Bush's conditions for signing the measure, or face a government shut-down like the 1995-96 debacle that wasted 27 days and was blamed on the party controlling Congress at the time. Back then, it was the Republicans; now, at least in the Senate, it is the Democrats.

As his price for letting Congress off this hook, the president wants defence appropriations to pass on time and a total budget closer to the House's \$759 billion than the Senate's \$768 billion. So the Democrats may find themselves going home—some of them, of course, to fight for their seats—►

Street furniture

Is nowhere safe?

NEW YORK

Advertising comes to Upper Manhattan's parking meters

FIRST it was buses, then elevators. Now New York city parking meters will be adorned with propaganda for films, clothes and computers. From October 1st, 500 parking meters on the well-to-do Upper West and Upper East Sides of Manhattan will carry advertising. If the ad spaces are filled all through the year, they could bring the city \$90,000—some help in reducing next year's projected \$5 billion deficit.

Each meter will be fitted with a three- or four-sided plastic unit, about half-

way down the pole, which advertisers will rent from Snap Marketing or Park Place Media. The city will receive roughly 10% of the revenue. Although officials have no say over content, "inappropriate" ads—for tobacco, alcohol, politics or sex—will not be allowed.

Council members and residents from the affected districts have already complained about aesthetics and respect for landmarks. As a result, meters in front of certain historic buildings must be ad-free. And several ad spaces will be designated for charities, public-service announcements and public art.

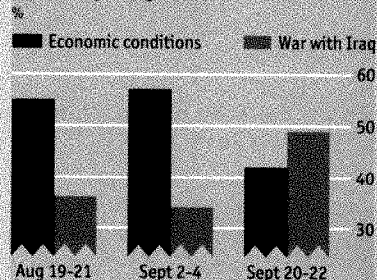
Some residents argue (this is New York, after all) that they should not have to pay to park at meters with ads, since taxpayers have already paid for the meters themselves. The city's Department of Transportation, which is overseeing the scheme, counters that other publicly-paid-for spaces, such as bus shelters, are already used in the same way.

Four years ago, Park Place Media launched a similar programme in Springfield, Massachusetts, and it is hoping to do so elsewhere in the country. Yet New York intends to proceed slowly before any more of its 64,000 meters are ad-clad. "We are trying to keep an open mind here," says Tom Coccola, the Department of Transportation spokesman. The ads are "not terribly unobtrusive."

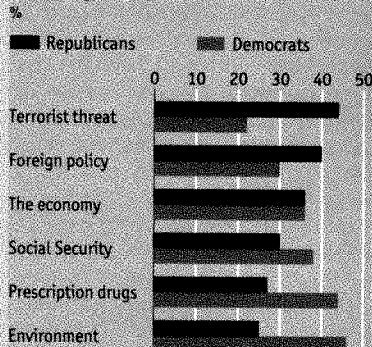


Competency test

Which of the following issues will be more important to your vote for Congress this November?



Which party can best handle...?"



Sources: Gallup; Pew Research Centre *Conducted Sept 12th-16th

▶ with a handful of Republican priorities and less than they wanted for health care, education and transport.

The Republicans have protected themselves against accusations of being cold-hearted on domestic issues by taking the initiative on a few key bills. House Republicans shepherded a prescription-drug benefit through their chamber in June, whereas the Democrat-controlled Senate only passed a bill to improve the availability of generic drugs, which will pull in fewer votes. The Republican-led House has also passed bills on pensions and welfare. The Senate Democrats were this week able to win over some moderate Republicans to their version of the homeland-security bill, which limits presidential control over federal workers. But this may be a hollow victory, because the Department of Homeland Security is now less likely to become law this year.

Will ordinary Americans notice such subtleties? A survey by the Pew Centre says that only 17% of them are paying close attention to the elections, and a quarter none at all. Anyway, it is not easy for the Democrats to change the subject from Iraq. A Gallup poll released on Tuesday suggests that Iraq is now a more important issue than the economy. One aspiring Democratic presidential contender, Senator John Edwards, said this week that soon Congress "will have dealt with Iraq and we'll be on to other issues." Even if that were true, it may be too late. ■

Drug wars

One puff at a time

The states are loosening drug laws; will Washington follow?

PROHIBITION supposedly divided America, like Gaul, into three parts: wets, dries and hypocrites. Cannabis is now doing the same. One in three adult Americans admits to having tried the herb; most have survived, and some have even gone on to become president. Yet the government still spends billions of dollars trying to save them from it. In 2000, the last year for which figures are available, 734,497 people were arrested on marijuana charges, more than twice the number in 1991. Nine in ten of these "criminals" were guilty of possession alone.

Several European countries have tired of this crusade. Will America follow? The first puff of smoke comes from Nevada, where a chance to legalise marijuana is on November's ballot. Even if Nevadans vote in favour of Question Nine, they will need to do so again in 2004 for the initiative to

Taxes

Sinning gets expensive

WASHINGTON, DC

Continuing bad behaviour spells good news for state budget deficits

ERROL FLYNN famously had trouble reconciling his gross habits with his net income. State governments have no such problem. Desperate to bring their massive (and constitutionally forbidden) budget deficits under control, they have been increasing "sin taxes" on such things as drinking, smoking and gambling. Nevada's proposal to tax cannabis (see main story) is merely the most daring of these ploys.

Sin taxes come in two kinds. In the first, the state taxes activities that are allegedly bad for you. In the second, the state itself gets involved in the activity and takes over part of it—by setting up a lottery, for instance.

Nowadays, states are rushing to do both. Tennessee, for instance, has an \$800m gap to plug in the fiscal year that ends on June 30th, 2003. It has just increased its cigarette tax by seven cents a packet (bringing in \$34.2m) and upped its alcohol tax by 10% (\$4.3m). A state lottery (\$200m) is on the November ballot.

Smokers are still the most battered sinners. According to the National Conference of State Legislators, politicians in 18 states passed \$2.9 billion in new tobacco taxes in the last fiscal year, accounting for nearly half of all new taxes passed. Some of the new taxes were at city level: New York city raised its tax per packet from eight cents to a whopping \$1.50. Each pack now costs about \$7.

Drinkers get less attention. Alaska and Tennessee were the only two states to pass an alcohol-tax rise this year, but 19 other legislatures have considered it. Several states already levy a betting tax, taking a cut from each bet. Nevada earned \$688m this way last year, and may raise the tax from its present 6%. Illinois and Indiana take in an extra \$400m a year between them.

Most states like to boast that some of

become law. Yet the aim is clear: to make pot as legal as beer.

Nevada has already moved a step or two in that direction. Two years ago, voters widely approved a measure to legalise marijuana for medicinal purposes. In 2001, the state legislature decriminalised possession of small amounts of the drug. Under Question Nine, anybody older than 20 would be allowed to possess up to three ounces of the stuff—enough for a nice evening in (or at least that's what some guy we met somewhere told us once).

The details of the distribution system



Siren song

the earnings from such taxes go to public programmes that are intended to discourage the activity in question. On the other hand, they don't want to tax the sin so hard that people stop sinning. One politician seems in earnest: Mayor Michael Bloomberg of New York is trying to ban smoking altogether in large restaurants and bars, suggesting that, for him, the bottom line is secondary to a crusade against the habit. Studies show that a 10% increase in the cost of smoking will lead to a 4% drop in the number of those doing it, rising to 6% among the poorer and less-addicted young.

Sin taxes alone will not cover most states' deficits. Combining all three of Tennessee's sin taxes would not produce half the sum needed. But nor is there much danger that receipts will fall, as long as human nature remains as it is.

are still unclear: would there be special shops and farms, or would anybody be allowed to grow and sell it? But the state legislature would regulate dealers, tax sales of the weed and even subsidise low-cost medical marijuana for some patients, such as AIDS sufferers. The initiative sets out harsh penalties for smoking the drug in public, selling it to children and driving under the influence. Anybody caught selling the drug without a proper licence would be sent to prison.

Advocates argue that a regulated marijuana market would free policemen for ▶▶

other work and give the government more control over the trade. Even the Nevada Conference of Police and Sheriffs, weary of the thankless task of pursuing pot-smokers, endorsed Question Nine at first—though it backed down when its endorsement made headlines, and its president had to resign.

A recent opinion poll shows Nevada's voters rejecting Question Nine by 55% to 40% (5% being unsure). It will probably be much closer than that. A record 110,000 people signed a petition to put the idea on the ballot, with 18-25-year-olds (surprise!) showing particular enthusiasm. Billy Rogers, campaign manager for the artfully named Nevadans for Responsible Law Enforcement, which is pushing the initiative, is confident that Question Nine will pass. This is despite the news that America's drugs tsar, John Walters, will descend on Las Vegas on October 10th to speak out against it. Although he will come armed with plenty of alarming statistics, the pro-cannabites feel his visit will only help their cause. Nevadans do not like federal bureaucrats telling them how to vote.

The state, which already allows legalised prostitution and gambling, may seem an atypically libertarian sort of place. But 11 states have decriminalised possession of small amounts of marijuana, and eight allow use of the drug for medicinal reasons (California, Colorado, Maine, Nevada and Oregon permit both). Recent national polls show 70% of Americans supporting medicinal marijuana and 60% favouring decriminalising possession of small amounts. A number of other ballot initiatives in November reflect this shift. Voters in Arizona will decide whether to decriminalise small amounts of marijuana; and in wide-open San Francisco, red-eyed voters may decide whether the city itself should

start growing cannabis.

The problem is how to reconcile these states' lenient laws with the stringent federal ones. Last October, the Bush administration began a wide-ranging crackdown on medicinal-marijuana distribution, tearing up patient-run gardens and confiscating doctors' files in California. A group of these doctors has successfully sued the government, though the case has gone to appeal and could eventually reach the Supreme Court. In Santa Cruz on September 17th, medical marijuana was handed out at City Hall in a protest against a federal raid on a cannabis collective. A States' Right to Medical Marijuana Act has attracted 36 co-sponsors in Congress, but seems unlikely to get anywhere this year.

Money may eventually help politicians to change their minds. It costs \$1.2 billion a year to keep 60,000 people in prison for marijuana offences. The cost in police time is stunning, too: California is said to have saved \$100m a year in enforcement costs by relaxing its laws. By letting Nevada tax the drug, Question Nine would turn the wicked weed into a nice little earner. ■

Stem-cell research

The rebel state

SAN FRANCISCO

California defies the president

CALIFORNIANS do not in general feel much warmth for their governor, Gray Davis. Now, however, the state's scientists feel a new glow. "He should be applauded," says Helen Blau, a professor of pharmacology at the Stanford University School of Medicine, and so say many others. The governor earned their approval by signing on September 22nd a bill which allows scientists in California to use embryonic stem cells in research. This is in direct defiance of federal limits on the practice.

Stem cells are the raw material out of which developing embryos fashion all the other cells that eventually form a body. Unlike specialised cells that devote themselves to one role—being skin, or making hormones, say—stem cells have the capacity to change into other kinds of cell. They offer a possible means of repairing tissue damaged by degenerative diseases.

But such research worries people who abhor the destruction of human embryos it involves. Many anti-abortion groups have campaigned against it. A bill to ban it altogether is deadlocked in the Senate (as is one that would allow it). The White House is sympathetic to a ban, and last year George Bush issued an executive order that restricted federal money for re-



A shrewd move from Davis

search to a limited number of existing stocks of previously harvested stem cells.

This federal disapproval has produced a rare brain-drain out of the country. Last year, Roger Pedersen, who led stem-cell research at the University of California in San Francisco (UCSF), left America for Cambridge University. Anxiety about funding has apparently discouraged others from picking up the work. Ms Blau says the limit on federal funding threatens to upset the balance between private and public research.

California's bill, which was introduced by Deborah Ortiz, a state senator who has championed cancer research, explicitly permits the donation and destruction of embryos for stem-cell research. Fertility clinics will be required to tell women that they can give to researchers discarded embryos generated by fertility treatments. Donated stem cells may be multiplied to give scientists more to work with.

Mr Davis has drawn the line somewhere; in another bill, signed the same day, he indefinitely extended the state's ban on reproductive cloning (the permitted research is for so-called therapeutic cloning, which might eventually allow failed organs to be replaced with new versions made from a patient's own cells). But he has still thumbed his nose at Mr Bush and drawn attention to the Republican Party's anti-abortion politics a month and a half before he fights for re-election. The White House looks uncomfortable. At first the president's spokesman said that, as a matter of states' rights, California's decision was of no concern to Mr Bush; but this was amended to say that the president disagreed with Mr Davis and that policies should "respect the culture of life".

The scientists hope to press their advantage. On September 25th, Ms Ortiz and Mr Pedersen appeared before a Senate hearing on stem-cell research. And California is feeling pleased with itself again. ■



Quick, the drugs tsar's coming

Lexington Ron Kirk's enterprise

A black Democrat is making strong moves to uproot the Republican Party from Texas



IN 1964, fresh from signing the Civil Rights Act, a glum Lyndon Johnson complained that the Democrats had just lost the South for a generation. Southern whites promptly confirmed his fears by switching to the Republicans in that year's presidential election. Today, all elected state officials in LBJ's native Texas are from the Grand Old Party, and his old Senate seat has been in Republican hands for 41 years.

Now, just possibly, the curse may be about to be lifted. LBJ's seat is currently up for grabs because of Phil Gramm's retirement. And an affable black Democrat called Ron Kirk is in with a chance of winning. Political races don't come more charged with symbolism than this.

If Mr Kirk wins, he will be an instant superstar: a man who broke the mould of southern politics, struck a blow for black power and gave George Bush a bloody nose in his home state. He will be the only black in the Senate, and only the third to sit in that august body since Reconstruction in the 1870s. He will also be the natural leader of America's black population. The Democrats would be hard-pressed to avoid putting him on their presidential ticket in 2008.

Mr Kirk has earned his reputation as a Democratic Colin Powell by running one of the country's most conservative cities, Dallas, for the past seven years. There, he endeared himself to the city's white corporate upper class by embracing business-friendly policies. This placed him firmly on the pro-business wing of the Texas Democratic Party, among such former luminaries as Lloyd Bentsen (Bill Clinton's first treasury secretary, and the man who gave Mr Kirk his start in politics), John Connally, a vigorous governor in Kennedy's day, and LBJ himself.

Mr Kirk showed his deal-making talent by pushing through a variety of projects—such as a downtown sports arena—that had been languishing for years. But he also proved that he was more than just a corporate schmoozer by working with the city's fractious council and keeping in with the city's black activists.

He is benefiting handsomely from the national interest in his candidacy, persuading his party to devote lots of resources to a state that it recently regarded as a black hole, and starring in fund-raisers in New York and Washington. He also gets some advantage from the fact that he is running on the same ticket as Tony Sanchez, an oil-and-banking tycoon who has so far spent

at least \$25m on his bid for the governorship—five times as much as his Republican rival—and could well end up spending double that. It would be hard to design a ticket better calculated to boost minority turnout without alienating whites.

This is clearly embarrassing for the Republicans. The last thing they want is a reputation for standing in the way of the state's first black senator and first Hispanic governor. But will it be enough to push Mr Kirk over the top? The smart money in Texas is that it won't: not quite and not yet. The Republican candidate, John Cornyn, may lack Mr Kirk's engaging personality and back-slapping manner. In fact, he may be a bit of a dull bird. But he is a solid enough candidate: a former state attorney-general and former state Supreme Court judge who is running a perfectly competent campaign. He also has the most valuable resource in Texas politics, the support of George Bush.

It is hard for people outside Texas to understand just how popular Mr Bush is in the Lone Star state. Hard-nosed businessmen go misty at the mere mention of his name; fresh-faced young Latinas enthuse about his moral values and solid leadership. Mr Bush is determined to avoid being bloodied by Mr Kirk. He is in the process of making a series of fund-raising visits to Texas, including one to Houston on September 26th. His wife Laura is drumming up support, particularly among suburban women. Karl Rove, an old friend of Mr Cornyn, and Karen Hughes, Mr Bush's former communications director—now back in Austin—are also doing their bit.

But Mr Cornyn got an unexpected boost last week, when Mr Kirk succumbed to a fit of Jesse Jacksonism on the subject of regime-change in Iraq. After pointing out that the people who will be doing the fighting will come largely from minority groups, he wondered whether the Republicans would be so keen to go to war "without any thought of loss" if the first half-million troops to go to the front came from millionaires' families. This jarred with the whites he still needs to enlist. It also exposed a contradiction at the heart of his campaign: the fact that he wants blacks to vote for him because of his colour and whites to vote for him regardless of it. An opinion poll taken after his faux pas showed him trailing Mr Cornyn by 12 points.

The post-civil-rights wave

Still, even if he loses, Mr Kirk's spirited campaign will remain important. He represents the rise of a new generation of pragmatic black politicians: a post-civil-rights generation that sees politics in terms of promoting economic growth which benefits everyone rather than looking for a confrontation with the white overclass. This generation is gaining momentum by the day: look at the careers of Harold Ford junior, the congressman for Memphis, Tennessee, and Shirley Franklin, the new mayor of Atlanta. If Mr Kirk fails, it will still only be a matter of time before another black reaches the Senate.

Mr Kirk also reminds Republicans that they can no longer take Texas for granted. Democratic-leaning minorities now make up 48% of the state's population. The booming high-tech sector lures in out-of-state professionals who have little time for fire-and-brimstone conservatism. Conservative areas such as Mr Bush's adopted home-town of Midland are mired in recession and losing population. The Republicans have already lost California, the mega-state that produced Richard Nixon and Ronald Reagan. Mr Kirk suggests that they may now also be in the process of losing the mega-state that produced the Bush dynasty. ■

ITU TELECOM ASIA 2002

Preliminary Forum Programme Overview

MORNING	MONDAY 2 DEC 09:00 – 12:30 PL1 R 201A+B JOINT FORUM OPENING Investing in Asia: From Recovery to Prosperity	TUESDAY 3 DEC 09:00 – 10:30 PL2 R 201A+B Investment Opportunities & Challenges 11:00 – 12:30 SA3 R 201A Asia & WTO: A) Challenges & Opportunities 11:00 – 12:30 SB3 R 201B Regulation & Market Dynamics 11:00 – 12:30 SB4 R 201B Telecom Regulatory Framework: Asia's Market Opening 10:00 – 12:30 TDS1 R 301B Access & Future Technologies: Broadband Internet Access	WEDNESDAY 4 DEC 09:00 – 10:30 PL3 R 201A+B Narrowing the Digital Divide: Moving towards IP 11:00 – 12:30 SA6 R 201A Asia & the Internet New Business Model 11:00 – 12:30 SB6 R 201B Critical IP-based Network Issues 11:00 – 12:30 SB7 R 201B Assessment of Asia's Progress in Opening Telecom Networks to IP 10:00 – 12:30 TDS2 R 301B Benefits to Citizens & Society: Internet for Development	THURSDAY 5 DEC 09:00 – 10:30 PL4 R 201A+B Wireless and the Digital Opportunity 11:00 – 12:30 SA9 R 201A Investing in Wireless 11:00 – 12:30 SB9 R 201B Leapfrogging the Digital Divide: The Impact of New Access Methods 11:00 – 12:30 SB8 R 201B Convergence and Services 10:00 – 12:30 TDS3 R 301B Implementation: ICT Regulation in 21st Century
	AFTERNOON 14:00 – 15:30 SA1 R 201A Boom, Bust, Build – Lessons learned & New Business Models (I) 14:00 – 15:30 SB1 R 201B Lessons learned going the Convergence Way (I) 14:00 – 15:30 SB2 R 201A The 3G Road to Success 16:00 – 17:30 SA2 R 201A Boom, Bust, Build – Lessons learned & New Business Models (II) 16:00 – 17:30 SB2 R 201B Lessons learned going the Convergence Way (II) 16:00 – 17:30 SB3 R 201A Delivering Content & Applications 14:30 – 17:30 YF R 301B Youth Forum: Technical	14:00 – 15:30 SA4 R 201A Asia & WTO: B) Market Opportunities 14:00 – 15:30 SB4 R 201B Dealing with New Issues 14:00 – 15:30 SB5 R 201B The New Regulatory Challenge 16:00 – 17:30 SA5 R 201A Investing in Next Generations: Markets, Businesses, People 16:00 – 17:30 SB5 R 201B Ubiquitous Access: Redefining Universal Service 16:00 – 17:30 SB6 R 201A Access-Capable Networks: The Role of the Internet of Things 14:30 – 17:30 YF R 301B Youth Forum: Policy & Regulation	14:00 – 15:30 SA7 R 201A IP Multimedia: Applications that will change the world 14:00 – 15:30 SB7 R 201B Developing Best Practices for e-government & e-governance 14:00 – 15:30 SB7 R 201A Government e-Governance in Asia 16:00 – 17:30 SA8 R 201A Diverse Broadband Access across the Region. What makes economic sense? 16:00 – 17:30 SB8 R 201B Evolutionary - Using the Internet to create new Digital Opportunities 16:00 – 17:30 SB9 R 201A Assessment of Asia's Progress in Opening Telecom Networks to IP 14:30 – 17:30 YF R 301B Youth Forum: Finance	14:00 – 15:30 SA10 R 201A Messaging beyond SMS 14:00 – 15:30 SB10 R 201B Broadband & Multimedia in Asia – Myth or Reality? Luxury or Necessity? 14:00 – 15:30 SB10 R 201A The Internet of Things 16:00 – 17:30 SA11 R 201A Billing, Service Assurance & Customer Service 14:30 – 17:30 YF R 301B Youth Forum: Technical, Policy & Regulation, Finance
PL TDS YF SA SB SC		MORNING FRIDAY 6 DEC 10:00 – 12:30 PL5 R 301A+B JOINT FORUM CLOSING		

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Dollarisation in Latin America

El Salvador learns to love the greenback

SAN SALVADOR

El Salvador is making a success of dollarisation. But that says as much about the country as the policy

WITH a population of 6m in an area the size of Massachusetts, El Salvador is a small country. But it is not an insignificant one. In the 1980s, its civil war drew the world's eyes. Having achieved peace and democracy a decade ago, it is now being closely watched by a more select group—aficionados of debates about exchange-rate policy. El Salvador is abolishing its currency, the colon, and adopting the dollar. If this succeeds in delivering higher growth, other Central American countries are likely to follow suit.

Two other countries in Latin America also do without their own currency. Panama has used the dollar since it broke away from Colombia, with American support, a century ago. In 2000 Ecuador adopted the greenback, as a desperate measure to stave off hyperinflation. A third country, Argentina, came close to dollarising when its currency's one-to-one peg to the dollar was assaulted by the markets last year, and may yet do so.

El Salvador's switch to the dollar has been a carefully planned policy, says Miguel Lacayo, the economy minister. The colon was pegged to the dollar back in 1994. Then, in January 2001, the currency began to be phased out. Today, 85% of transactions in the country are in greenbacks, and the dollar is the only unit of account in the financial system. The government expects the colon to disappear completely by the end of 2003.

Dollarisation may well make sense for El Salvador. Its economy, unlike Argentina's, is closely tied to that of the United States, which takes two-thirds of its exports. Some 2m Salvadoreans living in the United States send back almost \$2 billion a year in remittances—a sum equal to a seventh of GDP. Most Salvadoreans have been used to handling dollars for years.

El Salvador's economic policies have been geared to the change of currency. Since 1992, successive governments from the conservative Nationalist Republican Alliance party have pursued free-market reforms, privatising much of the economy. El Salvador has combined relatively high growth with low inflation (see chart on next page). Last year, after two devastating earthquakes, growth slowed to 1.8%. But that was still pretty good by most Latin American standards.

Salvadoreans have already started to benefit from dollarisation. The most obvious gain is lower interest rates. Consumer credit is growing. Companies and the government have been helped by cheaper international financing. And dollarisation has reduced transaction costs for firms.

But dollarisation also poses challenges. Although Guatemala has legalised the dollar as a domestic currency in parallel with its own quetzal, many of El Salvador's other neighbours and economic competitors have floating exchange rates. Their currencies have devalued. To remain com-

petitive, El Salvador has to respond with higher productivity and lower costs. Economic reforms have helped. Take telecommunications: after deregulation in the 1990s, there are now four competing telecoms firms, and charges have fallen. El Salvador also has an unusually flexible and energetic workforce. Foreign investors say this makes up for the second-highest labour costs in Central America.

Even so, there are worries. One is the government's budget deficit. Mainly because of the cost of rebuilding after the earthquakes, that rose to 3.7% of GDP last year. Unchecked, this risks driving up the cost of credit. The government has responded by cutting ministerial budgets by an average of 17% this year.

Businesses, too, have to be nimble. Ricardo Sagrera of Hilasal, a towel manufacturer, says that his firm has had to invest in new designs and production techniques to counter competition from Brazilian and Chinese rivals. GMT, which makes electronic parts for American assembly lines, faces a tougher challenge. Since 2000, its sales have slumped, and its workforce has shrunk from 225 workers to 80. The firm hopes to move back into profit by making more complicated parts, something its workforce can do but competitors, its owner Jaime Hill thinks, cannot.

In short, adopting the dollar is no panacea. To work, it requires deep structural reforms. That is a particularly tough test for Ecuador. Compared with El Salvador, not only is Ecuador's economy less closely linked to that of the United States but its inflation rate is higher, its labour market more rigid, and its economy still unreformed. Its government, too, is pretty profligate—and not because of earthquakes. Depending on who wins next month's presidential election, it is not impossible that Ecuador will end up dropping the dol- ▶▶

Also in this section

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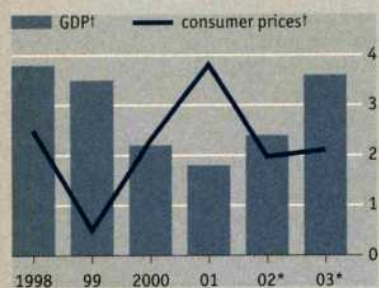
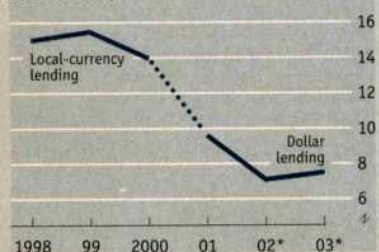
43 Mexico's oil troubles

43 Colombia's drug wars

Betting on the dollar

El Salvador's:

Interest rates, %



*Forecast 1% change on previous year
Sources: IMF; Economist Intelligence Unit;

▶ lar and launching its own currency again.

Even in El Salvador, not everyone is convinced. The main opposition party, the former guerrillas of the FMLN, has been against dollarisation. But a section of the party has broken away and formed a more market-friendly social-democratic group. In El Salvador, dollarisation looks irreversible. The fact that manufacturers like Mr Hill still support it shows that many Salvadoreans reckon the pain will be worth it in the end. If they are right, other Central American countries may soon be following in El Salvador's footsteps. ■

Canada, the United States and Iraq

Well, maybe ...

OTTAWA

Why the Canadian government can't make up its mind

IN THE old days, Canada was usually swift to join military alliances against aggressors. But the government of Jean Chrétien has been notably reluctant to make any public promise to join an attack on Iraq. George Bush's assertion that other countries must be either with or against America in its war on terrorism puts Canada on the spot. How could the superpower's neighbour and biggest trading partner be against? But, where Iraq is concerned, Mr Chrétien and his ministers have been arguing for military action only after seeking a fresh mandate from the UN.

This was the line Mr Chrétien took

when the two men met briefly in Detroit (significantly, a hub of cross-border trade) on September 9th. His deputy prime minister, John Manley, went further on September 20th when he said that Canada was unlikely to offer any "additional" military support without UN authorisation. When the foreign-affairs minister, Bill Graham, met Naji Sabri, his Iraqi counterpart, at the UN last week, he said that Canada wholeheartedly supported a tough UN resolution calling for unfettered access by inspectors to all weapons sites; but he has since refused to say whether Canada would support an American-led attack that went ahead without a specific Security Council mandate.

To some extent this wariness reflects Canada's familiar instinct not to want to seem just an extension of the United States. But it is also a reaction to the hesitation shown in opinion polls. Just before the Bush-Chrétien meeting, one poll said that 60% of Canadians thought their country had already given the United States enough support in its war on terrorism. Other surveys suggest that, although a majority of Canadians favour a joint military command structure in North America and support (marginally) a ground invasion of Iraq to change its regime, they doubt Mr Bush's reasons for changing it. Nearly 70% of Canadians also believe that the United States bore some responsibility for the September 11th attacks because of its Middle East policies.

For all that, Canadian forces are likely to be drawn indirectly into any conflict with Iraq, whether or not the Security Council sanctions it. Two Canadian frigates, a destroyer and maritime patrol aircraft are attached to the American aircraft-carrier groups in the Arabian Sea, and B-2 bombers starting from their Missouri base would need to fly through Canadian skies to attack Iraq. These commitments date from the Afghan campaign, and will not be withdrawn. Canada, however, does not want to repeat the experience of Afghanistan, where a Canadian battalion under American command spent futile weeks combing the mountains and in April an American plane mistakenly bombed Canadian troops, killing four of them.

So the Canadians are looking to Hans Blix, the head of the UN Monitoring, Verification and Inspection Commission, who is trying to field an inspection team in Iraq by mid-October. The problem is timing. Ron Cleminson, the Canadian commissioner with the UN inspection body, estimates that it will take up to ten months for inspectors to prepare a definitive report, even with, cross your fingers, full Iraqi co-operation. But the United States may not want to wait that long. Mr Graham foresees an American strike against Iraq in February's cool weather if Saddam's regime is not by then complying with the UN. ■

The mess in Paraguay

Plunging into misery

SAO PAULO AND ASUNCION

Paraguay blows its chance of a financial rescue

FACED with a three-day protest planned for this week, and after the violent suppression of a demonstration last week, President Luis Gonzalez Macchi, the head of Paraguay's corruption-riddled government, caved in. He partly reversed a recent rise in fuel prices. The transport strike called for September 25th was put on hold, but the government faces bankruptcy.

The protesters also seem likely to win the scrapping of proposed tax rises that the IMF had called for in return for a \$200m rescue loan. They are particularly angry that the austerity package the government had agreed on with the Fund was mainly about raising taxes, instead of cutting the inefficient and corrupt public sector, bloated with supporters of Mr Gonzalez's ruling Colorado Party. The bail-out, which James Spalding, the finance minister, had said was the government's only hope of staving off bankruptcy, now looks dead.

National income per head in this South American country of 6m people has been shrinking for seven years. More than half of the population lives in miserably poor conditions. And the depression has intensified this year. The currency, the guarani, has plunged by a quarter. Paraguay's farmers, the most important part of the economy, may fail to obtain new loans to finance this year's harvest: the banks, still waiting for some of last year's repayments, are refusing to give them more money unless the government guarantees the loans. Which, without money from the IMF, or somewhere, it cannot do.

The deeply unpopular Mr Gonzalez admitted this week that he might resign if his party asked him to do so. His vice-president, Julio Cesar Franco, should then take ▶▶



Things are looking up for Oviedo

over, but Mr Franco is also expected to resign soon, to seek his Liberal Party's nomination as presidential candidate in next April's election. His failure to do anything has in any case disappointed many Paraguayans, who contemptuously call him "flowerpot". There is now talk of installing a Supreme Court judge or a senator as stopgap president until the election.

Who can save Paraguay from plunging still deeper into misery? I can, says Lino Oviedo, a former army chief and serial coup-plotter who fled to Brazil in 1999 after being accused of arranging the murder of Luis Argaña, Mr Franco's predecessor as vice-president.

Alas, Mr Oviedo, for all his sins, is probably Paraguay's least unpopular politician, and might well win the presidency if he could run (a conviction over a 1996 coup attempt now disqualifies him). Instead, he is likely to put up a stooge to contest the coming election, hoping that the Supreme Court and Congress can then be quietly leaned on to grant him a full pardon, allowing him to come home triumphantly and run the country from behind the scenes. That many Paraguayans see him as their best hope shows what a dismal state the country is in. ■

Mexico's oil troubles

Pemexacerbated

MEXICO CITY

Why the oil workers are threatening an explosive strike

FOR the past two weeks, the streets of Mexico's main cities have been echoing to the sound of marching feet. The country's oil workers have been demonstrating in favour of a 15% pay rise, threatening to go on strike on October 2nd if their demand is not met. The nationalised oil monopoly, Petroleos Mexicanos (Pemex), has been offering only 5.5%.

As the deadline nears, the government and the oil union have upped their rhetorical exchanges, warning each other of grave risks if neither of them backs down. A strike would devastate the Mexican economy, as oil still provides the government with over a third of its revenue. The international consequences for global oil markets at a time of confrontation with Iraq could also be severe. With a production of over 3m barrels a day, Pemex is the sixth-largest oil producer in the world. It is also among the largest suppliers to the United States. Worry over the prospects of a strike partly accounted for the 3.5% fall in the peso last week. On September 23rd, the Bank of Mexico had to raise interest rates to shore up the currency.

Colombia's drug wars

Castaño's gamble

MIAMI

Carlos Castaño may be heading for jail

THE days of Carlos Castaño, the leader of Colombia's outlawed right-wing paramilitaries, appear to be numbered. Mr Castaño is being sought for extradition with two of his aides, accused of shipping 17 tonnes of cocaine to the United States over the last five years. The indictment, announced on September 24th, is part of the American administration's efforts to clamp down on the drug trade that fuels Colombian terrorism. This was also timed to coincide with the visit this week of Colombia's new president, Alvaro Uribe, to the White House.

Mr Uribe is hoping for more, and much needed, economic assistance as he steps up the war back home. Congress has already provided more than \$2 billion in the last three years. The Bush administration would like to give Mr Uribe as much help as it can, regarding him as someone who means business, unlike his two weak predecessors, Ernesto Samper and Andres Pastrana. But in order to get Congress fully on side, the Bush administration needs Mr Uribe to show some concrete signs of progress.

Capturing Mr Castaño would help. His arrest would also help silence those on the left who have long complained that Colombia has not done enough to rein in the paramilitaries, responsible for some of the worst atrocities in the country. As the leader of the outlawed United Self-Defence Forces of Colombia (AUC), Mr Castaño has operated with virtual impunity for more than a decade. Colombian military officers have been accused of providing tacit and sometimes



Me? A drug dealer?

active support to the group.

Curiously, Mr Castaño may be ready to turn himself in and says he is willing to stand trial in America in order to clear his name. Though claiming to oppose drug trafficking, he admits that his men collect as much as \$200m from taxes on drug producers. It is only money from drugs, he says, that enables his paramilitaries to maintain their fight against Colombia's left-wing FARC guerrillas. "In southern Colombia we have a narco-FARC", he said in one recent interview. "The paramilitaries can't live off rice." But living off drugs is a dangerous alternative. Otto Reich, the American State Department's top official for Latin America, says that the AUC is breaking apart because of its "internal contradictions". Now, he adds, "some groups of paramilitaries are more interested in drug-trafficking than the war."

However, this being Pemex, it is more than just money that has provoked the threat of a mass walkout for the first time since the company was founded in 1938. Long closely tied to the Institutional Revolutionary Party (PRI), which ruled the country for over 70 years until it was defeated in 2000, the union is also protesting against the new government's prosecution of its leader, Carlos Romero Deschamps, who is also a PRI member of congress. He is implicated in a scandal—known as "Pemexgate"—in which about \$170m of Pemex money was allegedly fed through the union to support the PRI's failed presidential campaign in 2000. On September 24th, congress authorised prosecutors to start procedures to strip the union leader (and two other PRI legislators and union officials) of their parliamentary immunity so that they can face criminal charges.

President Vicente Fox has pledged to press the case against the union officials as part of his wider commitment to get corruption out of Mexican politics. This is commendable, but the case has soured his relations with the PRI. Unfortunately for Mr Fox, he desperately needs the support of at least some of the PRI's people if he is to push forward his stalled reform agenda, since his National Action Party does not command a majority of the seats in either house of congress.

As *The Economist* went to press, Pemex and the union were trying to find a compromise. A full-blown strike is unlikely, partly because the union's leaders would not have the backing of all its members. But even a relatively small pay rise could push up wage inflation in other parts of the economy, just when the Bank of Mexico is anxiously appealing for restraint. ■



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Senator Mechai Viravaidya, Chairman,
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Sen. Viravaidya is one of the highly-acclaimed
leaders of Thailand. He led his country in major
reforms in information, infrastructure, economic
cooperation, tourism, population and rural
development. He was awarded the 1997 UN

Population Award and the 1994 Ramon Magsaysay Award for Public
Service.

Mr. Hernando de Soto, President,
Instituto Libertad y Democracia Lima, Peru

Mr. de Soto is a staunch believer in the
rule of law and property systems that
create capital and include the poor for
countries to achieve genuine development.
He wrote the book "The Mystery of Capital:
Why Capitalism Triumphs in the West and

Fails Everywhere Else," and was recently chosen as one of the five
leading Latin American Innovators of the Century by the Time
Magazine (May 1999). The Economist magazine rated the ILD as
one of the "world-wide most important think tanks".

Confirmed speakers for the conference include:

Alejandro Jadresic, Executive Director, Jadresic Consulting
and former Minister of Energy, Chile;

Areepong Bhooch-Oom, Director, Office of State Enterprise
and Government Securities, Ministry of Finance, Thailand;

Y.G. Muralidharan, Consultant, Consumer Advocacy
Karnataka Electric Regulatory Commission, India;

Rohan Samarajiva, former Director General of Telecommunications,
Sri Lanka and Visiting Professor, University of Delft, the
Netherlands;

Nazrul Islam, Executive Director and CEO, Infrastructure Investment
Facilitation Centre, Bangladesh;

Perry Rivera, Regulatory Director, Regulatory Affairs Planning
Manila Water Company, Philippines;

Dale Whittington, Specialist, Infrastructure Provision,
University of North Carolina

Other speakers who have been invited include:

Warick Smith, Manager, Private Provision of Public Services
The World Bank;

Manuel Pangilinan, Chairman, Philippine Business for Social
Progress, Philippines;

W. Greg Wood, Chairman, CPCS Transcom, Canada;

Visoot Phongsathorn, Principal Advisor, Advisory Services
for the Thai Government on Implementing the
Commercialization and Privatization of Public Sector
Institutions, Thailand

Some topics

**Monday, 28 Oct. 2002, Reaching the Poorest: Taking Stock
PPIAF and Asia**

Plenary 1: The Challenge of Using the Private Sector to Deliver
Infrastructure Services

Perspectives from Government and the Private Sector
The True Costs of Public Provision

Plenary 2: The Spread of Private Provision in Infrastructure:
Implications for the Poor

Corporate Social Responsibility - Reaching out to the Poor
Creating an Environment for Private Investment

Plenary 3: Lessons from Early PPI Projects

Caselets: Bangladesh and Public-Private Partnership on Road
Rehabilitation Operations and Maintenance

**Tuesday, 29 Oct. 2002, Expanding and Improving Options for Low-
Income Households**

Plenary 4: Introduction to Key Policy Levers

Plenary 5: Innovations in Market Structure
Case Study on Innovation in Distribution of Water to
Save the Poor

Case Study on Mobilizing New Entry - Telecoms

Plenary 6: Making Regulation Pro-Poor

Presentation on Regulatory System Design -
Lessons from Telecoms

Case Study - Electricity Regulation

Plenary 7: Rethinking Subsidies

Case Studies: Output Based Aid (Chile)

Subsidy Design in Transport

Subsidy Design in Electricity

Public Service Obligations - Building a Framework for
Government

**Wednesday, 30 Oct. 2002, Supporting Implementation: Pro-Poor Reform
Processes**

Plenary 8: Processes for Delivering Infrastructure Services to the Poor
Role of Private Sector in Delivering Infrastructure Services
- A "Pro-Poor" Process

Working with Poor Households and Communities in the
Reform Process: The Regulatory View
NGOs as Watchdogs to Ensure Delivery of Services to the
Poor

Closing Remarks: Role of Donors

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- Conference documentation - Cocktail
- Gala Dinner

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Israel and Palestine

Yasser Arafat amid the ruins

JERUSALEM

He is again under siege, but Israel's impolitic demolition of his compound has made a hero of the Palestinian leader

"IT'S just words," said an Israeli official, dismissing a reprimand from George Bush that was more remarkable for its rarity than for its severity. "He has to say them because of the coalition-building against Iraq." Mr Bush had told reporters on September 24th that Israel's destruction at the weekend of all but one of Yasser Arafat's government buildings in Ramallah had been "not helpful". Hours earlier, in another unusual expression of dissent from Israel's unremitting attack on Mr Arafat's regime, America abstained on a UN Security Council resolution demanding that Israel stop pulverising what remains of the complex, and withdraw "expeditiously" from Palestinian cities.

Will Mr Bush leave it at words? A spokesman at the State Department said that America wanted to see the UN resolution enforced, and that this desire was being conveyed to Israel. At the very least, the new, cool tone is likely to head off Israeli plans, leaked earlier in the week, for the physical elimination or enforced deportation of senior political leaders in the Islamist Hamas movement.

An overnight armoured raid into Gaza City on September 23rd, a harbinger, perhaps, of things to come, left nine Palestinians dead. Israel said that eight of them were armed fighters; the Palestinians insisted that only three of them were. Thousands of Gazans attended the funerals, demanding "revenge" rather than the largely

non-violent protests that have flowered lately all over the West Bank.

America, fighting for UN support on Iraq, plainly can do without further escalation in Palestine. But that was just as plain before Mr Sharon ordered his tanks and bulldozers into Ramallah on September 19th, after a gruesome bus-bombing, claimed by Hamas, in the heart of Tel Aviv. That atrocity killed six people, and injured 50, and could, some think, have caused the furious, spontaneous response.

But the demolition work in Ramallah was so patently impolitic and untimely—crushing the delicate international and domestic efforts to engineer some kind of Palestinian regime change, including divesting Mr Arafat of many of his executive powers—that only a conspiracy theory, it seemed, could rationally explain it.

Mr Sharon, some pundits surmise, does not truly want to see a more pragmatic Palestinian leadership evolving, because he would then be required, by Mr Bush for one, to negotiate with the new men over relinquishing the West Bank and Gaza. This is certainly the view held by some of his far-right and religious political allies. Better, according to the theorists, for Mr Sharon to keep Mr Arafat in place as a convenient punch-bag.

The renewed harassment of Sari Nusseibeh, a prominent Palestinian moderate, appeared to support the conspiracy theory. Mr Nusseibeh has drawn obloquy

from Palestinian radicals for his outspoken condemnations of terrorism, and his persistent advocacy of a return to negotiation. Yet, by order of Israel's minister of internal security, his offices in Jerusalem were raided, and then shut down, by the police.

Israel says its tanks and troops will continue to besiege Mr Arafat's last intact building until the Palestinian leader hands over several militants who, Israel now claims, are among the 200-odd guards and officials cooped up with him. The list is curious, including, for instance, Tawfiq Tirawi, a Palestinian intelligence commander who, earlier this year, was regularly holding talks with top Israeli generals and intelligence men.

The Palestinians are convinced that the assault on the compound is a bid to destroy what remains of the Palestinian Authority, and to undermine the nascent movement for its reform. Earlier this month, their newly appointed cabinet had been forced to resign rather than face a confidence vote it was bound to lose. Led by young deputies from Mr Arafat's own Fatah movement, the parliamentarians clamoured for the removal of several ministers long accused of corruption.

And, on September 19th, even as the bus was exploding in Tel Aviv, Mr Arafat was holding a meeting with senior Palestinians who wanted measures to be taken against the terrorists whose violence was in open defiance of Fatah's ban on attacks on Israeli civilians inside Israel. They also demanded that Mr Arafat should appoint his "deputy", Mahmoud Abbas (Abu Mazen), as prime minister in readiness for the elections that are supposed to be held in January. Mr Arafat supported the first demand. He was less enthusiastic about the second but, according to one participant "was not openly opposed".

These relative calm waters have now ►►

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► been replaced by turbulence. On the night of September 21st-22nd, thousands of Palestinians, by no means just the young and foolhardy, defied the curfew by taking to the streets of Ramallah and other West Bank and Gazan cities in pot-banging demonstrations. The Israeli army, apart from some wild shooting, in which five Palestinians were killed, mostly held its fire.

Mr Arafat, again under the barrel of Israeli guns, has regained his authority. After a meeting with other Fatah leaders in

Ramallah on September 24th, Mr Abbas was at pains to insist that nothing had been discussed other than the siege on Mr Arafat's office and how to end it. "There is no room for discussing the introduction of any changes in the structure of the Palestinian Authority, or creating new positions, at a time when the president is being subjected to the worst aggression," he said. And Mr Arafat was able to claim that the big West Bank demonstrations were "a referendum" on his leadership. ■

from Burkina and Mali, who make up much of Côte d'Ivoire's labour force.

By September 25th, forces loyal to Mr Gbagbo had regained control of Abidjan, the commercial capital, and had begun an attack on the second city, Bouaké, where rebels were hunkered down. The northern town of Korhogo was also under rebel control, and rebels were reportedly handing out guns to dissident youths. France, which keeps a permanent garrison in the country, was evacuating foreigners, including 170 mostly American children trapped in a mission school. Nearly 200 American troops flew in to help. Nigeria sent warplanes to assist the government; Ghana promised to follow suit.

The rebels sent a message, via the minister of sport, whom they captured last week, that they were willing to negotiate. A French consul is acting as an intermediary, and other African states are urging peace. But the defence minister says the government will not negotiate until the rebels lay down their arms, which they are doubtless too nervous to do.

Indeed, many Ivorians have cause to be nervous. Most opposition newspapers have stopped publishing, after the Ministry of Information gave warning that it could not guarantee their security if they published "articles embarrassing to the state". Foreign radio stations such as the BBC and Radio France International were taken off air on Sunday, and many journalists have fled their homes. The senior state broadcasting regulator said it was "quite usual" in wartime to "manage the media in order not to spread death and disruption among the populace." State radio is now giving out a number for people to call to denounce treasonous neighbours to the security forces.

The silencing of the press does not make it easier to figure out what is going on. Who exactly are the mutineers? The government says they are men who were recruited into the army when Mr Guei was president, but were about to be laid off, and did not want to be. Time will tell. Meanwhile, the government is furious at speculation that powerful people might have used the coup as a smokescreen to settle scores. Conspiracy theorists note that the murdered minister of the interior had enemies within the ruling party.

The only certainty is that Côte d'Ivoire's fraying reputation as an island of stability in West Africa has taken another heavy knock. From independence in 1960 until 1999, the country suffered no violent changes of government. Then Mr Guei seized power. The next year he was overthrown in a civilian uprising. Since then, the country has been cursed with plots, assassinations and ethnic fighting. As Mr Guei noted the week before he was killed: "Our poor soldiers don't even get time off any more...they're always on alert." ■



Côte d'Ivoire's mutiny

Coups, stratagems and spoils

ABIDJAN

Shaken by mutiny and murder, Côte d'Ivoire is a far cry from its old stability

THE president cancelled his audience with the pope and rushed home. Laurent Gbagbo, Côte d'Ivoire's pious strongman, was in Rome when, at 3am on September 19th, mutinous troops took to the streets of three Ivorian cities. Loyal soldiers swapped bullets and shells with the mutineers. Civilians cowered indoors, unable to tell whether the big-booted heavies outside their doors were shooting to topple the government or to defend it.

It is still not clear what happened, but here is a rough summary. At least 270 people died. The interior minister was killed, probably by rebels. Robert Guei, a former military ruler, was also killed. The government says he was behind the coup attempt, and died in a firefight as he made his way to the national television station to proclaim himself president. But state television showed the normally dapper Mr Guei lying dead on the side of the road in t-shirt and jogging trousers, with a single bullet hole in the side of his head. His relations say that he was murdered in his home, along with his wife, son and grand-

children. Mr Guei had been loudly critical of the government in recent weeks, calling it corrupt and oppressive.

Another prominent opponent of Mr Gbagbo's regime, Alassane Ouattara, was luckier. Troops burst into his home and killed members of his household, but Mr Ouattara escaped to the French embassy. His house was later ransacked and torched. Henri Konan Bédié, the last of the four Big Men of Ivorian politics, at first took refuge in the Canadian embassy, but then emerged and gave a press conference, siding with the government.

When Mr Gbagbo returned, he announced that "the hour of battle has struck" and threatened to unsheathe his blade against "traitors aided by a foreign rogue state" and, of course, "terrorists". Most Ivorians took this to mean that the coup was backed by neighbouring Burkina Faso, which that country's government hotly denies. Mr Gbagbo promised to clean up "insalubrious areas" of town. Paramilitary gendarmes then burnt down shanty-towns full of migrant workers

Burundi's civil war

The people want peace

BUJUMBURA

But the men with guns do not

TWO star-cross'd lovers stand on a small, green hill, fretting that their families hate each other. Mbazumutima and Natalie have been sweethearts since childhood, but his father was murdered by members of her tribe. Characters in "Our Neighbours, Ourselves", Burundi's most popular radio soap opera, talk a lot about tribal murder, because that, for Burundians, is reality. In 1993, the year Mbazumutima's fictitious father was killed, 250,000 flesh-and-blood Burundians were slain for real. A civil war continues to rage, pitting a government dominated by ethnic Tutsis against largely Hutu rebels.

But the programme does try to show how Hutus and Tutsis can get along, and if listening figures are anything to go by—almost everybody tunes in each week—ordinary Burundians crave peace as much as the programme's creators. The men with guns, however, are not good listeners. On September 22nd, peace talks collapsed after the main rebel group refused even to agree terms for a ceasefire.

Like Rwanda, its northern neighbour, Burundi has been bloodied by fighting between the majority Hutus and the Tutsi minority since its independence. Indeed, the 1994 Rwandan genocide was partly caused by the Burundian massacres of 1993. Bujumbura, the country's pretty capital, is periodically shelled by rebels, either from nearby hills or from gunboats on Lake Tanganyika. On September 9th, at least 183 Hutu villagers were murdered by the army, in reprisal for rebel attacks; the doomed peace talks were then put on hold for two days to allow the rebels to mourn.

Before giving up as mediator last November, Nelson Mandela, South Africa's former president, had some success in bringing the two sides together. He brokered a power-sharing agreement, the Arusha accord, between President Pierre Buyoya's government and several Hutu opposition parties, which produced a transitional government, but no ceasefire.

The rebels reject the transitional government as a poodle of the Tutsi leadership. They have a point. Mindful of what happened in Rwanda, Burundi's ruling Tutsis are afraid to surrender power. There are still no Hutu officers in the army, although thousands of foot-soldiers have been recruited. In May, Mr Buyoya is due to swap jobs with his Hutu deputy, Domitien Ndayizwey. But without a ceasefire, both men may feel too insecure to proceed.

The Hutu-Tutsi conflict is not as ancient as many outsiders suppose. It was deliberately fomented by the very groups now being asked to patch up their differences. The country has been ruled for most of the time since independence by a few Tutsis from the same hill in southern Burundi. Only by stirring up a race war have they managed to unite the rest of their small tribe behind them. The Hutu rebels, for their part, have split into a bewildering number of factions.

With international support, Mr Buyoya could yet defeat the rebels. Last year, South Africa sent 700 peacekeepers to protect members of the new government from the rebels. Rwanda, too, recently sent troops, for fear that Burundi's violence might spill across its border again. Tanzania, home to hundreds of thousands of Burundian refugees, might also send peacekeepers. On October 7th, these countries are to meet to discuss further action. ■

Morocco's election

The palace and the politicians

RABAT

The Interior Ministry calls the tune, but Morocco's voters are shy of dancing

IT MEANT it this time, said the Interior Ministry. Morocco's legislative elections on September 27th would be fraud-free and, under a new proportional-representation system, would produce the first real sounding of political sympathies.

The long-suffering Moroccan public had come to regard politics as a rather dan-

gerous activity for the man or woman in the street, and a rather profitable one for the individuals elected to parliament. Elections have long been rigged by high-level interference and local corruption. Moroccans were promised an honest election in 1997. But, that time, the centre-right Istiqlal Party claimed that it had been robbed of victory by behind-the-scene fixers. It was eventually coaxed into a broad Socialist-led coalition, but has vowed not to repeat this experience.

King Mohammed came to the throne in 1999 promising a new era of openness and democracy. But many of the high hopes that accompanied his accession have faded. The continued high unemployment, the alleged corruption in high and low places, and the shambolic public hospitals are among the main grumbles.

However, this week's vote is the first since Driss Basri, Morocco's interior minister for nearly 20 years and a master of electoral alchemy, was shown the door in late 1999. Driss Jettou, the current minister, is a mild-mannered former shoe manufacturer who heads a team of born-again democrats. They worry about the electorate's high level of illiteracy, which they, and others, see as a big obstacle to the creation of a credible legislature.

Another brake on progress is the score or so of small contenders, with names that typically include the words democratic, national, popular or reform. Once encouraged by the palace as a way of keeping the political landscape fragmented, the tiny parties are now an embarrassment. But most of them will fall at the qualifying threshold of 3% of votes cast.

Even so, the next government is bound to be another coalition, stitched together in discreet inter-party talks. This time, it could well be led by Istiqlal, and include the conservative Islamists of the Justice and Development Party.

The palace remains the final arbiter. The Interior Ministry, which some Moroccans say is the only one that counts, is in its keeping. Four other ministries, including foreign affairs, justice and Islamic affairs, are palace appointments. The king presides over meetings of this select cabinet, which operates in parallel with the prime minister's own cabinet, and takes most of the important policy decisions.

Many politicians chafe under this state of affairs, but none has so far felt ready to go public. And the average Moroccan needs to be convinced there are enough honest and capable politicians around before getting too excited about reclaiming decision-making from the palace. ■



Reading what Driss Jettou says

Correction In our article on Jordan and Iraq ("A Big Mac future", September 21st) we said that Le Royal hotel in Amman was built with Iraqi money. Actually, it is owned by General Mediterranean Holding, whose founder and chairman is Nadhmi Auchi. Mr Auchi is of Iraqi origin but now has a British passport.



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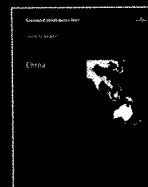
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Germany's general election

Gerhard Schröder clings on

BERLIN

The incumbent German chancellor has won a cliff-hanging election but with no real mandate for reform

IN ONE of the tightest German elections for half a century, Chancellor Gerhard Schröder's coalition of Social Democrats and Greens managed to cling on to power by its fingertips. Together the pair have 306 seats, a majority of nine in the Bundestag, the lower house of parliament. In the outgoing one, they had a majority of 21, and could usually count on at least the abstention of the 36 ex-communist Democratic Socialists who this time failed to clear the hurdle to obtain any seats by proportional representation and got only two directly elected seats.

Mr Schröder's slim majority will not only make it harder for his government to push through painful reforms but also puts a question-mark over its longevity. Previous governments, notably Helmut Kohl's after 1994, have had equally thin majorities yet have survived; a sitting chancellor can be displaced in mid-term only by a "constructive vote of no confidence", meaning that parliament has to vote for an alternative administration and not just ditch a beleaguered one.

Still, Mr Schröder will find the going tough. Discipline within the left-wing parties is often loose, particularly among the idiosyncratic Greens. The conservative opposition has gained ground. It already controls the Bundesrat, Germany's upper house, where about half of federal legislation has to be passed. And the economy is

continuing to stagnate. Edmund Stoiber, the defeated conservative challenger, says he expects the new government's life to be "very, very short".

On a night of nerves, with both leaders at different moments claiming victory, the two main formations—the Social Democrats and the combined Christian Democrats and their Bavarian sister party, the Christian Social Union—each got 38.5% of the vote. In the end, the Social Democrats piped the conservatives, by almost 9,000 votes and three seats. The new Bundestag is expected to have its first sitting in the week that starts on October 14th, with the formal re-election of Mr Schröder as chancellor on the same day or soon after.

With the Social Democrats losing ground since the previous election, in 1998,

it was the Greens who kept the ruling coalition afloat. They emerged as the election's only real winners, with 8.6% of the vote, their highest score since they first won seats in parliament in 1983. They are now clearly the country's third force.

Barely a year ago, after a string of electoral setbacks, they seemed tired, bland and on the way out. Mr Schröder had even begun eyeing the Free Democrats, Germany's liberals, as alternative coalition partners. But the combined effect of recent floods in the east (which revived many voters' environmental concerns), of the chancellor's stand against a war in Iraq, and of a strong campaign by Joschka Fischer, the Greens' foreign minister and Germany's most popular politician, helped them bounce back. Mr Schröder can thank the Greens for letting him keep his crown. In turn, they will now expect more influence, and say they will press the chancellor to raise the tempo of reform.

The liberals, despite doing a little better than last time, were the election's losers. Their expectations had been high. Pollsters throughout the campaign had put them ahead of the Greens. Only last month, one poll gave them 13%, double the Greens' ▶▶

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Just

Seats in Bundestag, 2002 (1998)

Social Democrats
251 (298)

Christian Democrats/
Christian Social Union
248 (245)

Greens
55 (47)

Democratic
Socialists
2 (36)

Free
Democrats
47 (43)

Source: Bundeswahlleiter

Party-list votes cast, % of total

Party	2002	1998
Social Democrats	38.5	40.9
Christian Democrats/ Christian Social Union	38.5	35.1
Greens	8.6	6.7
Free Democrats (liberals)	7.4	6.2
Democratic Socialists (ex-communists)	4.0	5.1
Others	3.0	5.9

projected score. They had begun to assume that no government could be formed without them. But they ended up with a modest 7.4%, a point behind the Greens and a far cry from the 18% they had set themselves. A renewed rumpus over anti-Israeli comments by Jürgen Möllemann was partly to blame. He has now resigned as the liberals' deputy leader. But the "fun party" image projected by their leader, Guido Westerwelle, though attracting young voters, may well have put off many of the party's older, more earnest supporters. Many Germans think Mr Westerwelle lacks gravitas.

Despite failing to hit all three of his proclaimed targets—to have the biggest group in parliament, to win more than 40% of the vote, and to topple the government—Mr

Stoiber has emerged beaten but unbowed. His conservatives upped their 1998 vote by more than three percentage points, while the Social Democrats dipped by a couple. In Mr Stoiber's Bavarian homeland, his party's share shot up by 10.9 points to 58.6%, its best score in nearly two decades. Indeed, with 9% of the total national vote, Mr Stoiber's Christian Social Union can claim to be Germany's third biggest party, ahead of the Greens. He says he has no intention of retiring quietly back to his home state but stands ready to take the chancellor's job should the government collapse.

Were it not for last month's floods in the east and the threat of an American-led war in Iraq, Mr Schröder would probably have failed to win a second term. Neither event was of his making, of course. But he ex-

ploited them both to his benefit. As a result, says Donald Rumsfeld, the American defence secretary, relations between Germany and the United States have been "poisoned". He refused even to talk to his German counterpart at this week's meeting of NATO defence ministers in Warsaw, and President George Bush failed to send Mr Schröder the customary congratulations. The chancellor is eager for reconciliation and has even asked Britain's Tony Blair to help. But he insists that there will be "no change" in his opposition to Germany's participation in an attack on Iraq, even under a United Nations mandate.

This, says Mr Schröder, is "a difference of opinion" that should be accepted among friends; the relationship, he insists, is "intact". That is not the view in Washington (see page 36). Matters were not helped last week by the German justice minister, who was accused of lumping Mr Bush with Hitler by saying that the American president has sought to distract voters from problems at home by talk of war-tactics, she is said to have added, that were once used by "Adolf Nazi". She has denied making the remarks, but says she will resign anyway. Relations between the countries, and between Mr Schröder and Mr Bush, who have not talked since June, remain strained.

It is on the home front, however, that Mr Schröder faces his hardest task. Speeding up Germany's dismal growth rate, creating jobs and loosening the country's labour rigidities should be his top priorities. But the election does not suggest that the German people have an appetite for radical reform. Mr Schröder has no mandate for it. Nor would Mr Stoiber, if he had won. That is the election's gloomiest lesson. ■

Belgium's language wars

Tongue lashings

BRUSSELS

Rows over who should speak in which tongue have got worse

THE tensions between Dutch- and French-speakers are usually a source of private grief to the Belgians. Now their never-ending row has gone international. The Council of Europe, a human-rights watchdog which groups together 44 European countries, has rebuked Belgium for violating minority rights. How come?

The problem has its roots in the sensitive area around Brussels where the French-speaking Walloons and the Dutch-speaking Flemings live side by side. The Flemings harbour a special grievance about the city, for it was once predominantly Flemish, and some Flemings still ▶▶

The poll in Germany's east

A final communist collapse?

ROSTOCK

In Germany's east, the party that once ran the show may be dying

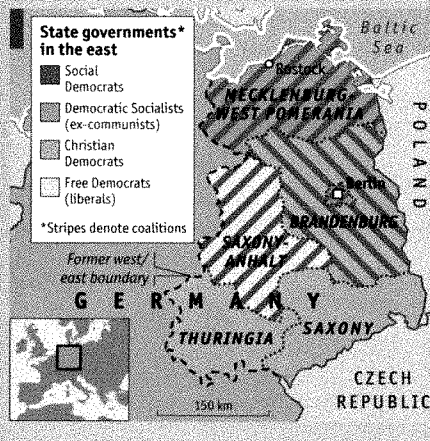
"MECKLENBURG-WEST POMERANIA is turning into a high-tech state!" boomed the stocky bearded man on the platform. "It'll be the best place for business in eastern Germany!" The loyal crowd huddling under umbrellas in the beautifully restored medieval market-place of Rostock, on the Baltic coast, looked bemused. Most of them like their Social Democratic state premier, Harald Ringstorff, a former chemist, and have nothing against his coalition with the ex-communist Democratic Socialists, though it aroused controversy when it was created four years ago. But the idea that the economy of the northernmost of the former East Germany's five states is forging ahead strikes the crowd as laughable.

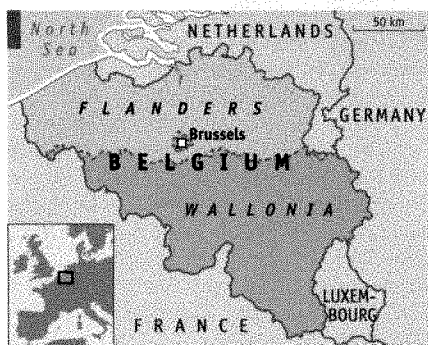
Last year it shrank by 0.8%. Unemployment stands at 18%, the same as when Mr Ringstorff took office. Yet in the state election, held on the same day as Germany's general election, 41% opted

for his Social Democrats, six percentage points more than in 1998. Though the Democratic Socialists' vote fell by eight points to 16%, Mr Ringstorff's "red-red" coalition is intact.

In the general election, the Democratic Socialists did badly throughout the former communist east. Their share of the vote there fell from 22% in 1998 to less than 17%. In the west, they polled a mere 1%, the same as in 1998, giving them an overall nationwide score of 4%, a percentage point below the threshold normally required to enable a party to form an official group in the Bundestag, Germany's lower house of parliament. If the ex-communists had won three individual seats despite failing to cross the 5% national threshold, they could still have retained the right to an allocation of seats in proportion to their total national vote. But they won only two directly mandated seats—so that will be their sole tally in the new parliament. In 1998, when they polled just 5.1% nationwide, they were granted 36 seats, despite winning only four directly elected ones.

Is this the beginning of the end for the heirs to East Germany's communist rulers? It looks that way. Their participation in ruling coalitions in the city-state of Berlin as well as in Mecklenburg-West Pomerania has deprived them of their identity as a protest party. Their failure to make a mark during last month's floods in the east sullied their image as the area's true guardians. And the resignation in July of Gregor Gysi as Berlin's economics minister over an air-miles scandal robbed them of a star. It is chilly without one.





hope it may yet be the capital of an independent state of Flanders. But demographic change means that 80% of its inhabitants now speak French. This has made the Flemings all the more determined to insist on the use of Dutch in the Flemish areas around the city.

If you live anywhere in Flanders, they say, you should speak Dutch—with no exceptions for the 120,000 Walloons living in Brussels's periphery. All local council proceedings must be in Dutch, even in a couple of communes where the mayor and most local politicians are Walloon. All official letters must, in theory, be sent out only in Dutch. Libraries stocking too many French books will lose their subsidies. Walloons who turn up at local councils unable to speak Dutch must bring translators. This infuriates the francophones, since they are quite sure the officials behind the counter can speak French. "We can speak your language, so why don't you learn ours?", the Flemings respond.

For some years a group of Walloon protesters around Brussels has been indulging in civil disobedience. Some refuse to speak Dutch in local shops. Others won't pay local taxes on the ground that the demands are written in Dutch. In 1998 some Walloons had the bright idea of petitioning the Council of Europe. An investigator concluded that Belgium should sign the European convention on minorities' rights, to bolster Walloon rights. But nothing happened. So the Council of Europe has written another report, scolding Belgium for ignoring its earlier recommendations. The council's parliamentary assembly was due to debate the issue this week.

Relations between Belgium's two main groups are anyway more fraught than usual. The national government almost broke up recently when Flemish Greens threatened to resign from the government (one of them did) in protest against arms exports to Nepal from a factory in the Walloon bit of Belgium. The Council of Europe report will stir more bad blood but won't help the Walloons. Though Belgium has now signed the council's convention on protecting minorities, all seven of its regional and national parliaments have to ratify it to give it legal force. But do not expect the Flemish parliament to sign up. ■

Spain and the Basques

An ugly mood

MADRID

Spain struggles to silence the party that speaks for Basque terrorism

BANNING the political mouthpiece of the Basque separatist terrorist group, ETA, is proving a mixed blessing. Security people in Madrid point hopefully to some big recent setbacks suffered by the terrorists and say that the political ban on Batasuna, ETA's hitherto legal political arm, is helping to throw the terrorists on the defensive. Politics, however, is another matter. Relations between the government in Madrid and the non-violent Basques who run their own regional government have rarely, if ever, been worse.

In the security field, the picture brightened a fortnight ago when two top terrorists were nabbed in France. ETA has been slower than usual to hit back with its usual reply—more terrorism—and seems likelier nowadays to botch its operations. Earlier this week, two terrorists accidentally blew themselves up in Bilbao, the region's biggest city. For sure, the killers have not entirely lost their lethal skills. The day after that accident, a booby-trapped Batasuna banner in another Basque town killed a civil guard, bringing the number of ETA's fatal victims this year to four. But that is far fewer than in the mid-1980s, when ETA was killing nearly 100 people a year.

In any event, Basque politics, both in the region and in Madrid, the Spanish capital, have become a lot more complicated. In particular, the main non-violent Basque party, the Basque Nationalists, better known by their initials PNV, who run the region's government, fiercely oppose the ban on Batasuna. Hence the ill-feeling between the region's rulers and Spain's national government in Madrid, run by Jose Maria Aznar and his conservatives.

Moreover, the procedure for banning Batasuna is proving by no means simple. That is because there are two prongs to the process. The first is being wielded by Baltasar Garzon, a prominent judge, who took the initiative last month to suspend Batasuna in the name of one of Spain's highest courts. The second is being wielded by the government in Madrid, which must prove that Batasuna should be banned under a specially amended law on the obligations of political parties which it recently enacted with Batasuna in mind.

To complicate matters more, the non-violent PNV, who run the region, are not entirely at one. The Basque premier, Juan Jose Ibarretxe, did his best to obey Mr Garzon's order that Batasuna's headquarters be closed down. But the PNV's veteran

leader, Xabier Arzalluz, is more belligerent—and more loth to co-operate. He has likened Mr Aznar's policy towards the Basques to that of General Franco, who clamped down ruthlessly on Basque (and Catalan) nationalists. Mr Ibarretxe and his government, however, are still trying to keep within the new law—by challenging Mr Garzon's ruling in higher courts.

But the Basque regional assembly, also controlled by the PNV, has gone a step further than Mr Ibarretxe's Basque government by declaring Mr Garzon's ruling invalid. So it is refusing to suspend the assembly's Batasuna members, who still enjoy their parliamentary privileges.

That in turn has prompted calls in Madrid, mainly by conservatives but by some Socialists too, to suspend part or all of the self-government Basques enjoy under the system of regional devolution enshrined in the post-Franco constitution, which makes provision for this if a region "fails to meet its constitutional or other legal obligations and poses a serious threat to the general interests of Spain". Mr Aznar says that his government has not yet contemplated taking so drastic a step. But some of his supporters are pressing him to do so.

"We never said the ban was going to be a panacea," says one of Mr Aznar's aides. "But it is morally right." The government argues that, after years of giving way to nationalist demands, it is time to defend the rights of those in the Basque region who want it to stay fully part of Spain and are subjected to intimidation and violence by the separatists. The PNV ripostes that when the current constitution of 1978 was approved in a referendum, it abstained. Since the moves to ban Batasuna, such differences between non-violent politicians over how the Basque country should be run have become even more bitter. ■



ETA's serpentine mural message

Ireland's coming EU referendum

Still nerve-racking

DUBLIN

This time the Irish seem likely to say yes. But you can't yet bank on them

"SAME bad treaty! Don't be bullied! Vote No to Nice!" says the blunt message on the poster tied to the lamppost outside parliament in Dublin. The words are set against the backdrop of a man with a gun pointed at his head. They refer to the treaty that was agreed upon by the European Union's 15 governments in December 2000 but rejected by Irish voters in a referendum in June last year. On October 19th, they will vote on it once again.

At stake for the EU are its plans for taking in up to ten new countries, mostly from Central Europe, and for streamlining the

EU's decision-making methods to cope with the influx. The other 14 countries already in the club have all ratified the treaty. Only Ireland's endorsement is lacking. At stake for Ireland, say Irish advocates of a yes vote, is their country's place in the EU. It must either remain at the heart of European decision-making or find itself isolated and friendless at the margin.

Since being rebuffed by Ireland in the first referendum, the EU has declared that its proclaimed common foreign and security policy will not force traditionally neutral countries, such as Ireland, into becoming part of a new European defence axis. But the Irish government is focusing its campaign less on the merits of the treaty and more on Ireland's overall future in Europe. It is stressing the economic gains of membership more zealously, and warning voters that a second rejection could threaten Irish jobs by deterring foreign investors. It points out that in Ireland's 30 years in the EU it has become rich, with

GDP per head now at 122% of the Union's average. Yet the country is still a net beneficiary of the EU budget—this year to the tune of some €1.5 billion (\$1.5 billion).

Fianna Fail, the main party in the newly re-elected centre-right coalition government led by Bertie Ahern, is spending ten times more on the referendum campaign than it did last time. And the pro-treaty side has drafted in some big guns, such as former European commissioners, Peter Sutherland and Ray MacSharry, and the European Parliament's current Irish president, Pat Cox, to pep up its supporters.

This intensified yes campaign is paying off—so far. Polls give the treaty's supporters a two-to-one advantage. If there is a danger, it is that the government itself is having an unpopular spell and that on referendum day voters might choose to punish it by voting against Nice.

Many voters are annoyed by what they see as a series of post-election U-turns on spending. Earlier this month Mr Ahern decided to scrap his longstanding plan for a state-financed national stadium, known popularly as "the Bertie Bowl", leaving taxpayers with a hefty bill for costs already incurred. This week the finance minister, Charlie McCreevy, who had promised during the election campaign in May that "no cutbacks whatsoever are being planned, secretly or otherwise", was embarrassed by the leak of a confidential plan for cuts worth €900m in the next budget.

All this has undermined the government. Even the opposition parties that support the treaty have told their voters not to use the referendum as a chance to punish the government by voting no. ■

Slovakia's election

Phew! The winner lost

BRATISLAVA

An alliance of the respectable keeps out a dangerous old roughneck

A THUGGISH populist topped the poll. A smarmier, less belligerent one was third. But a group of four more respectable parties on the centre-right (one of them also populist and untested) won just enough seats between them to form Slovakia's next government. That, for a country striving to join mainstream Europe, is reckoned a stirring success.

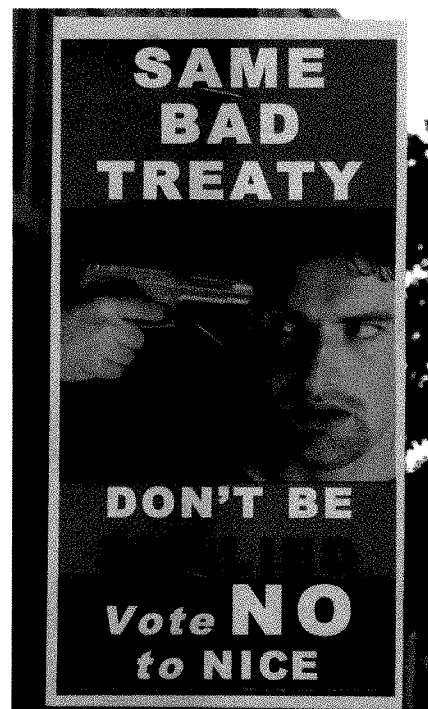
The party led by Vladimir Meciar, the strongman who woefully misruled Slovakia from 1993 until 1998, came top in a general election for the fourth time in a row since Slovaks and Czechs divorced nine years ago, but he has again been kept out of power because no other party has any wish to team up with him. As a result, Slovakia looks set to be invited, later this year, to join both NATO and the European Union.

All the same, it is a gloomy fact that nearly half of all Slovak voters plumped for populist or nationalist parties whose credentials are, to say the least, dodgy. Mr Meciar got nearly 20%, down from 27% at the last general election four years ago and from the 35% he won just after the split from the Czechs. So his popularity is undeniably dipping. Robert Fico, a younger, slicker and more stable version of the volatile Mr Meciar, came third with nearly 14%. The unreformed Communist Party got 6%, winning seats for the first time in post-communist Slovakia's history by doing especially well in the country's decrepit east, where unem-

ployment is sky-high. A nationalist party and a group that had splintered from Meciar's lot won 7%, though both failed to cross the 5% threshold needed to get seats in parliament.

Still, the centre-right fared more robustly than expected. The Democratic and Christian Union of Mikulas Dzurinda, the incumbent prime minister, came second with 15%. He is expected to team up with an ethnic Hungarian party, which got 11%, the Christian Democrats with 8%, and the Alliance of New Citizens, known by its acronym ANO (meaning Yes), a new outfit on the right headed by Pavol Rusko, a television magnate, which also got 8%. This reform-minded four-way coalition (similar to the last one, plus ANO) will have 78 seats in parliament, giving it a majority of three. Mr Dzurinda is expected to stay on as prime minister, though some say his foreign minister, Edward Kukan, could displace him.

Most democratic-minded Slovaks are heaving a sigh of relief, mainly because their country's bid to join the West now looks likely to succeed. Beyond that, though, all is not well. Corruption among Slovakia's ruling politicians and leading businessmen is rife. Disgruntlement is widespread. The protest vote was big. Mr Dzurinda, or whoever runs Slovakia, has little time to lose if the populists are to be kept at bay in four years' time—or perhaps a lot sooner.



Concentrating Irish minds



Turkey's coming election

The front-runner mustn't run

ANKARA

Banning the country's most popular politician may give his party a boost

ONLY last month, Turkey's European friends were cheering the country's habitually squabbling MPs after they had voted for a big batch of reforms to make Turkey much more democratic. But their optimism has been dented by last week's decision of the country's electoral board that the man tipped to be the next prime minister cannot run for parliament.

According to the board, Recep Tayyip Erdoğan (above), who leads the newly formed Justice and Development party, or AK, which means "white" or "clean" in Turkish, cannot run because of a past conviction for reciting verses that, the judges said, "incited religious hatred". No matter that the poem was penned 90 years ago by a nationalist poet and is taught in schools.

And no matter, apparently, that the scope of free speech was much broadened by last month's constitutional changes. Hikmet Sami Türk, the former justice minister who helped to draft these new laws, says they expunged Mr Erdoğan's past offence. But the fierce head of Turkey's appeals court, Sabih Kanadoğlu, insists that under Turkish law Mr Erdoğan has been banned from politics for life—and that's that. For the same reason, Murat Bozlak, leader of Turkey's biggest pro-Kurdish party, HADEP, has been prevented from running for parliament. So has Akin Birdal, a leading human-rights campaigner. These harsh decisions might be sustainable but for the fact that the board has given the electoral go-ahead to a number of unsavoury characters, such as Oral Celik, a convicted drugs smuggler.

It is true that Mr Erdoğan began his career in an openly Islamist party that railed against the West. "My frame of reference is Islam," he proclaimed. But since being

AIDS in Russia

A looming plague

ST PETERSBURG

Russia is hopelessly ill-prepared for the coming epidemic of AIDS

ANDREI now realises it was a mistake to tell his dentist to don surgical gloves before tackling his tooth. It was an even bigger one to admit he was HIV-positive. The dentist simply refused to operate. Andrei now says that in future he will keep his condition secret, even if that puts others at risk. "If I try to be considerate, I get discriminated against. What choice do I have?"

Three years into what may be the world's fastest-growing HIV epidemic, Russia can offer victims only discrimination and despair. Since 1998, the number of registered HIV cases in the country has jumped almost 20-fold, from some 11,000 to nearly 200,000 in May this year. Compared with Africa, this sounds low. But the real Russian figure may be between three and ten times higher. The state health agency puts the number of infected people at 1m, some 80% of them under 30.

Russia's worst-hit city is St Petersburg. At the end of 2001 it had registered more than 17,000 cases; local health authorities say 97% of them are drug-users. But some experts say the number of cases in the city is about three times higher.

St Petersburg is one of the few places in Russia where the authorities have let non-governmental organisations conduct free, anonymous HIV tests and distribute syringes and condoms. A group called Doctors of the World is the largest outfit trying to reach the city's prostitutes, most of whom take heroin. Its head, Alexander Tsekhanovich, believes infection among drug users has peaked;

it is now spreading through sex. But Russia offers little sex education and promiscuity abounds. Researchers from the University of North Carolina found last year that 44% of teenagers had not used a condom last time they had sex.

Russia's decrepit health system is at a loss. Most doctors are frightened of being infected. Discrimination against HIV-positive people is rampant. Their condition is marked down in the "medical passports" which companies still demand from job applicants; few employers want them. Doctors sometimes refuse to treat them. A recent poll found nearly one-third of Russians wanted to quarantine people with HIV.

As in Africa, anti-retroviral therapy, which helps postpone the onset of AIDS, is generally thought to be too expensive, at around \$1,000 a month per person. In St Petersburg only about 100 people, mostly medical staff infected in the course of their work, receive it. Most medical workers now undergo HIV tests several times a year. So do pregnant women, soldiers and prisoners. Only in St Petersburg are tests more common: some 700,000 people, about every seventh inhabitant, receive annual tests.

The first big wave of AIDS-connected deaths will probably hit Russia in 2007 or so. By then, it is feared, some 2-3% of its people will be HIV-positive. So far the medical service is hopelessly ill-prepared. "Being HIV-positive in Russia is not a diagnosis," says one of St Petersburg's leading AIDS doctors. "It's a sentence of death."

forced out of his job as mayor of Istanbul in 1998, and spending four months in jail over the affair of the poem, he has changed his tune. First he broke ranks with Necmettin Erbakan, his old mentor, who was Turkey's first Islamist prime minister and was himself shoved out of power in 1997 by the country's meddlesome generals. Then Mr Erdoğan set up AK. And now he says he wants Turkey to join the European Union, stay cosy with the United States, and stick to a huge fiscal-reform package being financed by the IMF. He insists he is not, and never has been, an Islamist.

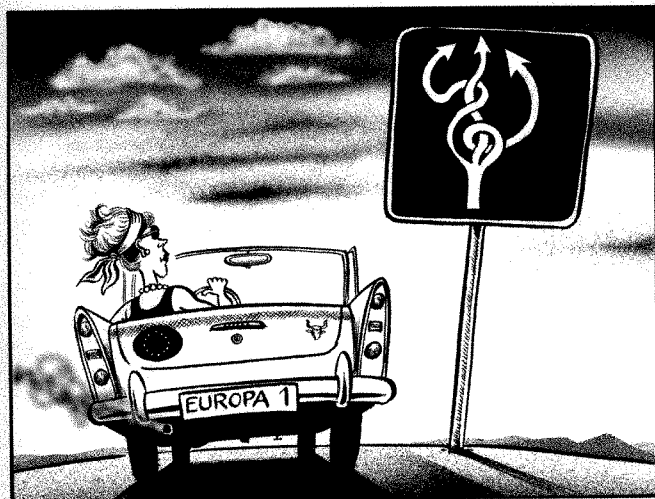
Whether or not most Turks believe in his conversion, a lot of them clearly think Mr Erdoğan is fit to run Turkey. Opinion polls consistently suggest that AK might get 25-30% of the vote—a good ten points more than its closest rival, the stodgily secular Republican People's Party. Mr Erdoğan

has promised to keep campaigning and has refused to name a successor to lead his party in the election fray.

His exclusion may even draw extra sympathy votes for AK, perhaps even give it an outright majority in parliament. That would be a nightmare not only for the army but for some of Turkey's industrialists, who live mainly in the Istanbul area and have for decades grown fat on the patronage dispensed by the crooked politicians of the country's mainstream parties. AK, they fear, might favour the more ostentatiously religious sort of businessmen in the Anatolian hinterland, who have been chipping away at Istanbul's economic dominance since the time of the late Turgut Özal, Turkey's visionary leader in the late 1980s and early 1990s. Banning Mr Erdoğan could have precisely the opposite effect to what the generals intended. ■

Charlemagne Left, right, left

Why political taboos are being broken in Europe



THE Germans invented the word *Zeitgeist*, but anyone hoping that their latest election would confirm a new “spirit of the age” in Europe will have been disappointed. In the past year or so, a clear trend seemed visible. Left-wing governments were ousted by the right in Italy, France, the Netherlands, Denmark, Portugal and Norway. Germany looked like the next and biggest domino to fall. But though Gerhard Schröder’s “red-Green” coalition wobbled, it refused to topple. Just the week before Mr Schröder’s victory, Sweden’s Social Democrats also bucked the trend, easily winning another stint in office. Now Austria’s Social Democrats have a chance of regaining power later this year. So much for Europe’s inexorable move to the right.

The broader truth, however, is that on the big economic and social issues facing Europe the differences between centre-right and centre-left—between Christian democracy and social democracy—are pretty paltry. Certainly the right is still closer to business, the left to the trade unions. But the resulting differences in policy have more to do with nuance than deep philosophy. In Germany, for example, Edmund Stoiber on the right proposed a top rate of income tax of 40%, while Mr Schröder wants to bring it down to 42%. Mr Stoiber said the state should consume no more than 40% of GDP, Mr Schröder stuck to his own favourite number, 42%. Economists and businessmen may clamour for a drastic revamp of Germany’s generous welfare state and for decisive moves to tackle public pensions, but neither candidate was prepared to risk suggesting anything daring. As Mr Stoiber drily remarked, he had not noticed anyone demonstrating for a radical overhaul of social security.

What is true of Germany is true of the rest of Europe. Italy’s Silvio Berlusconi admires Margaret Thatcher but has done nothing to tackle Italy’s pensions problem and little to free up the labour market. France’s new centre-right government has moved cautiously to mitigate the worst effects of its Socialist predecessor’s introduction of a 35-hour week but is committed to an extensive welfare state and shows no desire to take on the unions.

Faced with such tiny differences between left and right on the big issues of social and economic management, voters tend to plump for the most appealing personalities. One big reason why Mr Schröder and Sweden’s Goran Persson won while Lionel Jospin, a French socialist, lost is that the winning pair are

highly effective politicians while Mr Jospin came across as dull and stiff. Tony Blair’s mastery of British politics relies at least as much on his personality—and his Schröder-like sense of what people want to hear—as on any particular policies.

It was Mr Blair who made the last real attempt to define a new pan-European (and indeed transatlantic) political *Zeitgeist*. When the centre-left held sway on both sides of the ocean, he earnestly pushed forward his big idea—“the third way”. Mr Schröder tried briefly to echo him with cosy talk of a “new middle”. But the whole Blairite philosophy was too vague to catch on and much of the European left disliked what little it understood of it, assuming it was code for a kind of soft-edged Thatcherism. Mr Blair has now almost given up talking about the third way. In a recent interview in *Prospect*, a British magazine, he was reduced to claiming that “in parts of Latin America [the third way] is seen as a ground-breaking moment.” (They speak of little else in the queues outside Argentina’s banks.)

But while a welfarist consensus may still hold sway across the European Union, consensus politics are fraying around the edges in other ways. The most striking recent trend has been the rise of populist parties openly hostile to immigration. When Austria’s People’s Party became the first such party to join a governing coalition, there was outrage across the EU. But the rise of politicians making similar appeals elsewhere in other EU countries has muted the outcry. The Pim Fortuyn list in the Netherlands and Umberto Bossi’s Northern League in Italy have both joined governing coalitions after campaigns that highlighted the supposedly bad effects of immigration. The new centre-right Danish government relies on the votes of an anti-immigration party. As Bertel Haarder, Denmark’s immigration minister, points out, there may be a connection between addiction to welfare and hostility to immigrants. Partly because of high minimum wages and welfare benefits, there are very few jobs for unskilled immigrants: around 60% of them in Denmark have no job. So they are easily stigmatised as free-loading parasites.

Mainstream politicians have reacted in different ways to the rise of anti-immigration parties. In France the National Front’s Jean-Marie Le Pen won close to 20% of the votes in the presidential election but remains firmly beyond the pale. The new French government has nonetheless begun to toughen both rhetoric and actions against illegal immigrants. All across the EU, asylum-seekers are getting a frostier welcome.

Vox populi, a pox on civility?

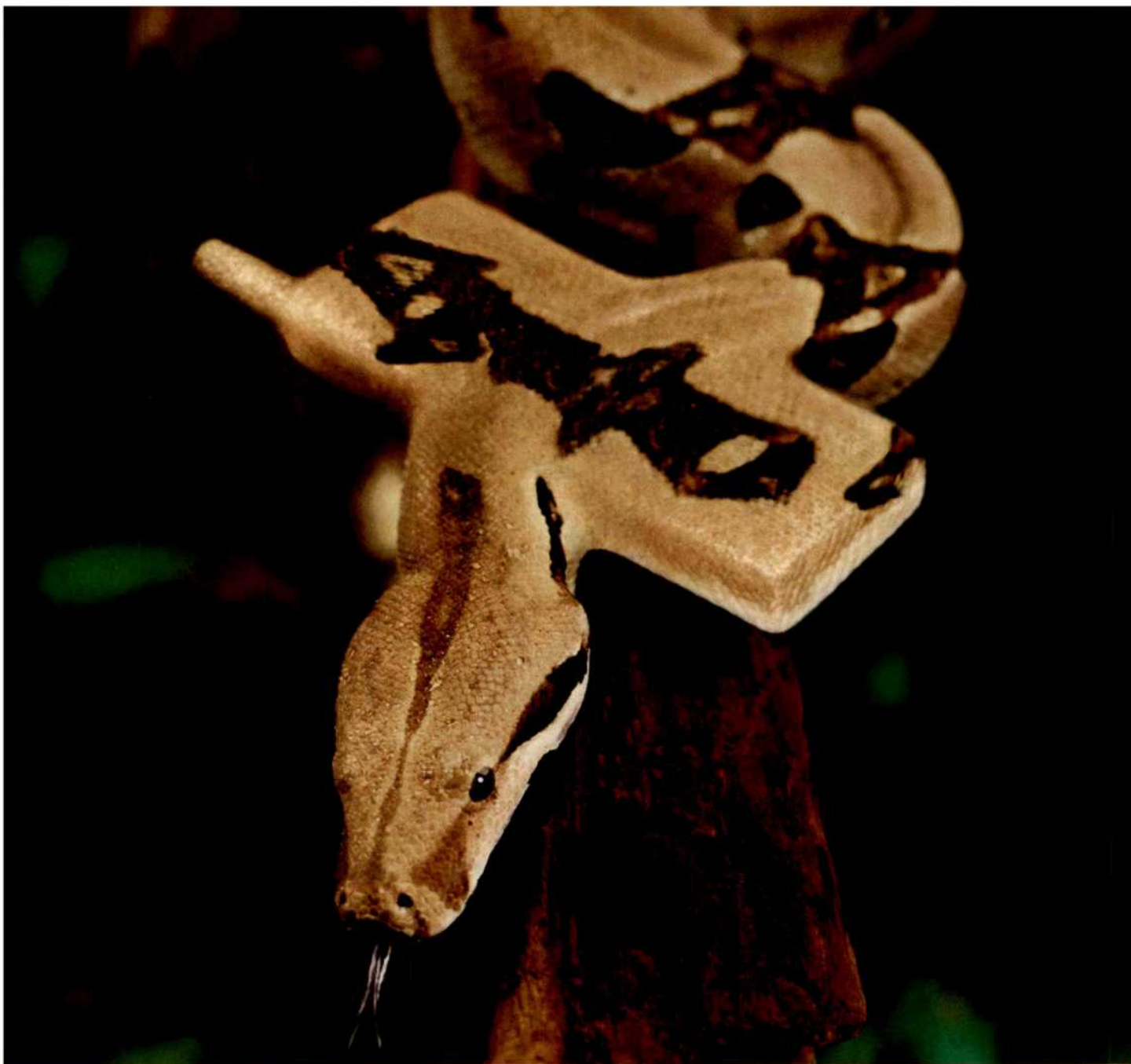
The rise of anti-immigration populists has demonstrated the political potential of voicing sentiments often heard in the street but rarely in parliamentary chambers. Mr Schröder’s campaign was a variation on this theme. Struggling in the polls, he decided to express the anti-Americanism that is a strong current of public opinion in Germany and the rest of the EU. Warning against “adventures” in Iraq and carping at the American economic model was just a mild version of commonplace feelings. Mr Schröder’s supporters took the hint—and helped him cling on to power. However, as with the immigration debate elsewhere in Europe, once a political taboo is broken it is hard to control the consequences. German relations with America have nose-dived. And new and queasy-making sentiments are popping out of the closet at home, such as the ill-fated comparison between George Bush and Hitler allegedly made by Mr Schröder’s justice minister. Sometimes taboos are there for a reason. ■

The
Economist



The unfinished recession

A survey of the world economy / September 28th 2002



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The unfinished recession

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Bubble and squeak

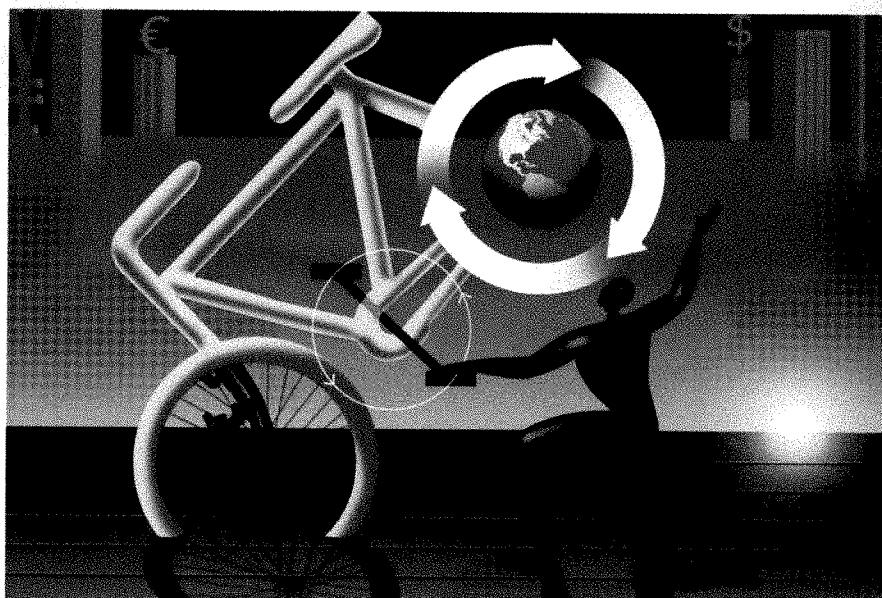
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After the bubbles

Brace yourself for a bumpier time ahead. Page 28



Obituaries for the business cycle were premature. Indeed, economies could become more volatile again over the coming years, argues Pam Woodall, our economics editor

"IT'S only when the tide goes out that you can see who's swimming naked." This famous remark by Warren Buffett, America's best-known investor, is a perfect description of what is happening in the American economy at present. The bubble in the late 1990s masked excessive borrowing by firms and households, widespread accounting fraud and the incompetence of company bosses, but now the effects of irrational exuberance and infectious greed are being shockingly exposed. Share prices have suffered their steepest slide since the 1930s. The tide has well and truly receded.

Yet most economists are still predicting robust economic growth of 3-3.5% over the next 12 months. Many of these are the same economists who in the late 1990s dismissed the idea that America was experiencing a bubble, and who insisted only last year that the economy was not heading for a recession. They were wrong then and are likely to be wrong again. America's economic downturn is not yet over. A protracted period of slow growth—perhaps even a further slump in output—is likely to expose more financial embarrassment of the Enron and WorldCom sort.

This is no normal business cycle, but the bursting of the biggest bubble in America's history. Never before have shares become so overvalued (see chart 1 overleaf). Never before have so many people owned shares. And never before has every part of

the economy invested (indeed, overinvested) in a new technology with such gusto. All this makes it likely that the hangover from the binge will last longer and be more widespread than is generally expected.

Three-way split

America's mild recession last year followed its longest unbroken expansion in history. The euro area, now in its ninth year of growth, has escaped outright recession, but has seen a sharp slowdown. In contrast, Japan's economy has suffered three recessions since its own bubble burst at the beginning of the 1990s. This survey will consider what the varying fortunes of the big economies reveal about the changing nature of the business cycle.

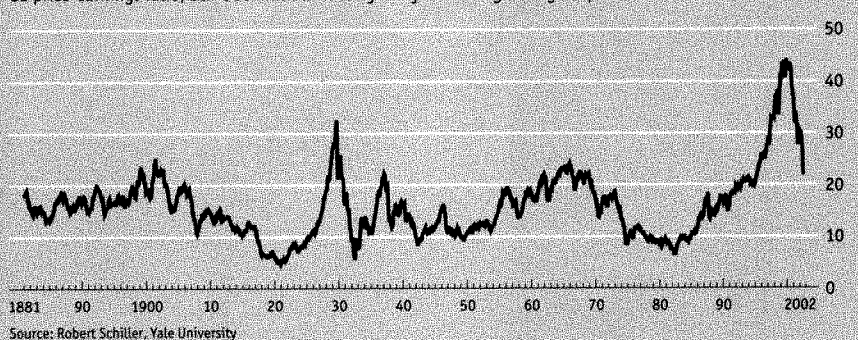
Views about governments' ability to tame the business cycle have themselves moved in cycles. In the 1950s and 1960s it was widely believed that Keynesian demand-management policies could stabilise economies: a slight touch on the brake or the accelerator was all that was needed. But the stagflation of the 1970s produced a new economic consensus that governments were powerless to do anything except restrain inflation. The business cycle returned with a vengeance: America had three recessions between 1974 and 1982. However, since then it has enjoyed two long booms, in the 1980s and again in the 1990s, interrupted only briefly by a mild downturn, leading many to believe that re- ➤

Sources

This survey draws on many sources and interviews, not all of them cited in the text. The author would particularly like to thank Adam Posen at the Institute for International Economics; Lakshman Achuthan at the Economic Cycle Research Institute; Victor Zarnowitz at the US Conference Board; Wynne Godley at the Cambridge Endowment for Research in Finance (CERF), University of Cambridge; Bill Martin at UBS Global Asset Management; and economists at the BIS, the IMF and the OECD. A full list of sources can be found on *The Economist's* website.

Bubble trouble

US price-earnings ratio, S&P 500 index divided by ten-year moving average of profits



Recessions were a thing of the past.

The "death" of the business cycle has often been exaggerated. In the roaring 1920s, just before the Great Depression, firms and investors thought the good times would never end. In the late 1960s, after what was then the longest expansion in history, America's Department of Commerce, deeming the business cycle to be defunct, changed the name of one of its publications from *Business Cycle Developments* to *Business Conditions Digest*, only for the expansion to end a year later. Again, in the late 1990s the "new economy" was thought to be immune to the business cycle, thanks to information technology, more flexible markets and globalisation. Yet economies, like drunks, continue to move in wavy lines.

Receding recessions

The business cycle is not dead, but it does appear to have become more subdued. During the past 20 years, the American economy has been in recession less than 10% of the time. In the 90 years before the second world war, it was in recession 40% of the time. In most other economies, too, expansions have got longer and recessions shorter and shallower. The exception is Japan, which in the past decade has suffered the deepest slump in any rich economy since the 1930s.

The revolt against Keynesian policies since the 1970s was based on the belief that government intervention destabilises the economy. However, America's recent experience shows that the private sector is quite capable of destabilising things without government help. The most recent bubble was not confined to the stockmarket: instead, the whole economy became distorted. Firms overborrowed and overinvested on unrealistic expectations about future profits and the belief that the busi-

ness cycle was dead. Consumers ran up huge debts and saved too little, believing that an ever rising stockmarket would boost their wealth. The boom became self-reinforcing as rising profit expectations pushed up share prices, which increased investment and consumer spending. Higher investment and a strong dollar helped to hold down inflation and hence interest rates, fuelling faster growth and higher share prices. That virtuous circle has now turned vicious.

Since March 2000 the S&P 500 index has fallen by more than 40%. Some \$7 trillion has been wiped off the value of American shares, equivalent to two-thirds of annual GDP. And yet share prices still look expensive. Martin Barnes, an economist at the Bank Credit Analyst, a Canadian research firm, estimates that over the 40 years to 1995 the S&P 500 traded at an average of 15 times historic operating profits; today the ratio is 20. Moreover, experience shows that markets generally overshoot on the way down: at the trough of the previous bear market in 1982, the S&P 500 traded at only eight times profits.

For corporate America, the recession has been far from mild: profits and business investment have suffered their steepest decline since the 1930s. But despite the collapse in share prices, the economy as a whole has so far held up much better than expected. Consumer spending has remained strong, partly thanks to rising house prices that have offset some of the equity losses suffered by households. By refinancing their mortgages, households have been able to borrow more against the increased value of their homes. But debt cannot rise faster than household income forever. Eventually households will be forced to save more and spend less.

Optimists cling to the fact that growth in labour productivity remains strong,

which should help firms to restore profits as well as ensure robust long-term growth. The slide in the stockmarket, they argue, largely reflects a crisis of confidence in corporate governance and accounting fraud, not deep-seated economic problems. They need to get some spectacles.

Diminishing returns

It is true that America has benefited from faster productivity growth since the mid-1990s (although the rise is less than once thought). But as with all previous technological revolutions, from railways to electricity to cars, excess capacity and increased competition are ensuring that most of the benefits of higher productivity go to consumers and workers, in the shape of lower prices and higher real wages, rather than into profits. Equity returns are therefore likely to be a lot lower over the next decade than the preceding one.

Mr Barnes reckons that investors will be lucky to see an average real return on equities of 5%, compared with 25% in the four years to 1999. As a result, households will need to save much more towards their pensions, which will drag down growth. And if the profitability of investment in IT turns out to be significantly lower than expected, investment will remain much weaker than in the late 1990s, eroding productivity growth.

The unwinding of America's economic and financial imbalances has barely begun. Share prices are still overvalued by many measures. Companies still need to prune much more excess capacity. Most worryingly, debts still loom dangerously large. Although much of the increase in reported profits in the late 1990s was illusory, the increase in corporate debt to finance that unprofitable investment was horribly real. Dresdner Kleinwort Wasserstein, an investment bank, estimates that American corporate balance sheets are more stretched than at any time during the past half-century.

American households' net worth is likely to shrink again this year, for the third year running, after a long, uninterrupted rise since the second world war. If lower share prices cause households to increase their saving sharply, America could be pushed back into recession. Even if saving rises more gradually, the economy is headed for several years of below-trend growth. A weaker dollar would help to cushion the economy, but only by squeezing growth in other countries. The rest of the world, which benefited so handsomely from America's speculative binge, »

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▶ will now have to share its hangover.

American short-term interest rates are already at their lowest for 40 years. If the economy went back into recession now, the Fed would have little room to cut rates. Recession would reduce inflation from its already historically low level of around 1%, raising the risk of a deflation along Japanese lines. Falling prices would increase the real debt burden, reduce spending and so push prices even lower.

The bursting of a bubble is much riskier when inflation is low, and inflation in America today is even lower than it was in Japan in the early 1990s. Even if America escapes deflation, low inflation will mean that wages and profits grow more slowly, making it harder for firms and households to work off their debts.

Vicious cycles

Over the past decade investors, firms and consumers put far too much faith in the power of information technology, globalisation, financial liberalisation and monetary policy to reduce volatility and risk. IT, the very sector that was supposed to smooth out the business cycle through better inventory control, has ended up intensifying the current downturn.

In principle globalisation can help to stabilise economies if they are at different stages of the cycle, but the very forces of global integration are likely to synchronise economic cycles more closely, so that downturns in different countries are more likely to reinforce one another. Financial

liberalisation is supposed to help households to borrow in bad times and so smooth out consumption, but again it is a two-edged sword: it also makes it easier for firms and households to take on too much debt during booms, which may exacerbate subsequent downturns.

Alan Greenspan is widely considered a highly successful chairman of the Federal Reserve, but the belief that he has special powers to eliminate the cycle is foolish. In July 2001 Mr Greenspan himself said in testimony to Congress: "Can fiscal and monetary policy acting at their optimum eliminate the business cycle? The answer, in my judgment, is no, because there is no tool to change human nature. Too often people are prone to recurring bouts of optimism and pessimism that manifest themselves from time to time in the build-up or cessation of speculative excesses."

Indeed, speculative excesses in asset prices and credit flows might occur more frequently in future, thanks to the combined effects of financial liberalisation and a monetary-policy framework that concentrates on inflation but places no constraint on credit growth. The current conventional wisdom that central banks will reduce economic and financial instability by keeping inflation low and stable is flawed. Low inflation is no guarantee of economic stability.

If the Fed had increased interest rates sooner in the late 1990s, America's economy might now be in better shape. Some economists worry that it may be making a

similar mistake now by allowing low interest rates to encourage a rapid increase in house prices and mortgage borrowing. The Fed may be offsetting the bursting of one bubble by inflating another.

This survey will analyse the causes of recessions, examine whether economies are becoming more or less volatile and ask what policymakers can do to prevent downturns. It will also explore the controversial idea that recessions are a necessary, sometimes even desirable feature of economic growth: they purge the excesses of the previous boom, paving the way for the next expansion.

Its two main conclusions will not make comfortable reading. They are, first, that after decades of declining economic volatility in developed economies, the business cycle is likely to become more volatile again over the coming years; and second, that America's "recession", defined as a period of growth significantly below trend (and hence accompanied by rising unemployment), is far from over. Until America's excesses have been purged, robust growth is unlikely to resume.

The job of policymakers is ideally to curb the build-up of speculative excesses. If they fail, then their task is to ensure that recessions do not become too deep, rather than try to prevent them altogether. Such efforts simply leave large economic imbalances. An economy that has been on a binge will inevitably suffer indigestion. Stuffing it with yet more credit is unlikely to aid its recovery. ■

Of shocks and horrors

The causes of booms and busts

IN THE bible, Joseph tells the pharaoh to expect seven years of plenty followed by seven lean years. That was, perhaps, the first documented business cycle—and the first (and probably last) example of an accurate economic forecast. Recorded data on business cycles go back to the early 19th century, but economists still cannot agree about what causes contractions and expansions in economic activity.

Economists have come up with all sorts of explanations, from the effect of sunspot activity on climate to the alignment of planets and their magnetic forces. The current preference is to look for more down-to-earth causes, which come in two main

varieties: those that explain the business cycle as a self-perpetuating process, and those that blame recessions on shocks or policy mistakes. The main theories are:

- **Exogenous shocks.** Recessions, it is argued, are caused by unexpected events, such as the rise in oil prices in the mid-1970s or, as some (incorrectly) tried to argue, the terrorist attacks on September 11th last year. If so, recessions are, by definition, totally unpredictable. They cannot be prevented, but once they have arrived governments can use fiscal and monetary policies to cushion demand.

- **Keynesian theory.** John Maynard Keynes blamed recessions on the inherent

instability of investment caused by "animal spirits": swings in the mood of producers, from optimism to pessimism. As investment slumps, jobs and household incomes fall, amplifying the initial drop in demand. Unemployment rises because workers will not accept the pay cuts required to price the jobless back into work. So, to bring the economy back to full employment, the government needs to pursue expansionary policies.

- **Real business-cycle theory.** This theory, which emerged in the early 1980s, sees productivity shocks as the cause of economic fluctuations. For example, if productivity falls, current returns decline, says ▶▶

the theory, so workers and firms choose to work less and take more leisure. Rather than explaining the cycle in terms of market failure, as Keynes did, real business-cycle theory views a recession as the optimal response by households and firms to a shift in productivity. If so, there is no point in governments stimulating the economy. But most economists find this theory hard to swallow. Mike Mussa, a former chief economist at the IMF, and now at the Institute for International Economics, describes it as "the theory according to which the 1930s should be known not as the Great Depression, but the Great Vacation."

• **Policy mistakes.** The late Rudi Dornbusch, an economist at the Massachusetts Institute of Technology, once remarked: "None of the postwar expansions died of old age, they were all murdered by the Fed." Almost every recession since 1945, with the exception of last year's, was pre-

ceded by a sharp rise in inflation that forced central banks to raise interest rates. The first mistake was to allow economies to overheat; the second to slam on the brakes too hard. This theory gave rise to the popular belief that recessions could be avoided so long as governments pursued prudent monetary policies to keep inflation low and stable. Yet the recessions in Japan after the 1980s bubble and America more recently suggest that price stability does not prevent booms and busts.

• **Austrian business-cycle theory.** This is the oldest, developed by Austrian economists such as Ludwig von Mises and Friedrich Hayek in the early 20th century. Unlike Keynes, who thought recessions were caused by insufficient demand, these economists put them down to excess supply brought about by overinvestment. As a result of mutually reinforcing movements in credit, investment and profits, each

boom contains the seeds of the subsequent recession and each recession the seeds of the subsequent boom.

According to Hayek, output fluctuates because the short-term interest rate for loans diverges from the "natural" or equilibrium interest rate—the rate at which the supply of saving from households equals the demand for investment funds by firms. If central banks hold interest rates below this rate, credit and investment will rise too rapidly, and consumers will not save enough. This creates a mismatch between future output (which will increase as a result of higher investment) and future spending (which will fall as a result of lower saving today). Cheap credit and inflated profit expectations cause both overinvestment and "malinvestment" in the wrong kind of capital. The mismatch between saving and investment will eventually push up interest rates, making some

Defining the R-word

What is a recession?

WHEN your neighbour loses his job, it is called an economic slowdown. When you lose your job, it is a recession. But when an economist loses his job, it becomes a depression. This old joke probably contains a grain of truth about the way economists perceive the severity of recessions. But what, exactly, are they?

According to a popular rule of thumb, recessions are defined by at least two consecutive quarters of declining GDP. However, the National Bureau of Economic Research, America's official arbiter of recessions, takes a more sophisticated approach. A recession, it says, is "a significant decline in activity spread across the economy, lasting more than a few months, visible in industrial production, employment, real income and wholesale-retail trade." The NBER's recession-dating committee does not actually look at GDP figures, because they come out only quarterly, not monthly, and are continually revised. Last year's figures initially showed that output fell in only one quarter, but revised figures now show three consecutive quarters of decline.

The NBER defines a recession as an absolute decline in economic activity. However, some economists view it as a period

when growth falls significantly below its long-term potential. This makes more sense where an economy's potential growth rate shifts over time, or when comparing economies that are growing at different speeds. Suppose country A has a potential growth rate of 4% and country B one of only 2%. A growth rate of 2% in country A will cause unemployment to rise, but in country B it will leave unemployment unchanged. By this definition, country A would be in recession.



The Japanese have long defined a recession as below-trend growth. By that definition, they suffered several recessions between 1950 and 1992 even though during that period their country's GDP fell in only one year. Their average annual growth of under 1% in the 1990s, compared with over 4% in the 1980s, makes their decade-long recession as deep, by this gauge, as in many economies during the Great Depression. The snag with this definition is that potential growth rates are devilishly hard to estimate. An easier definition of a recession is a drop in GDP per head. This would allow for the fact that America's population is rising, whereas Japan's and Europe's is flat, so slow GDP growth in America can leave the average person worse off.

The choice of measure makes a huge difference when comparing the severity of recessions. Suppose that America's potential growth rate is 3.5%, as the optimists claim, and that the economy grows by an average of less than 2% a year over the next few years, as this survey will suggest it might. If so, the total shortfall in output relative to potential over the four years to 2004 would amount to 8% of GDP, making this the worst recession since 1945.

previous investments unprofitable. Too much capacity will also reduce profits. Investment collapses, ushering in a recession. As excess capacity is cut, profits rise and investment eventually recovers.

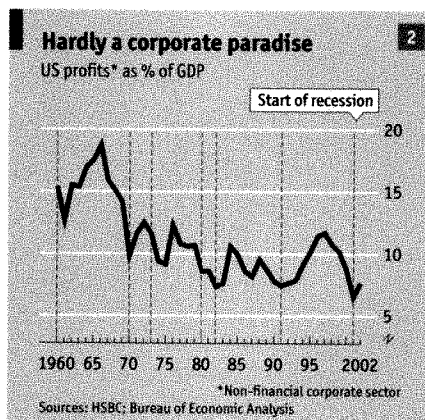
According to this theory, central banks would not be able to avoid a downturn by heading off a rise in interest rates. The only way to prevent the cycle from turning is to inject ever more credit, which becomes unsustainable. A recession is inevitable, and indeed necessary to correct the imbalance between saving and investment.

A tour of the Austrian Alps

In the second half of the 20th century, self-perpetuating theories of the business cycle were almost completely ignored in favour of theories that stressed shocks or policy mistakes. Most recessions were caused largely by economies overheating, forcing central banks to raise interest rates. Now, however, the fall in inflation has brought the inherently cyclical behaviour of credit, investment and profits to the fore.

In the late 1990s inflation rose only slightly, leading most economists to believe that growth would continue in America. Only a few economists, such as John Makin, at the American Enterprise Institute, and Stephen King, at HSBC, recognised that this cycle was different: that it was an investment-led boom that carried the seeds of its own destruction.

The recent business cycles in both America and Japan displayed many "Austrian" features. Hayek argued that the natural rate of interest could rise if faster productivity growth increased expectations about profits and hence investment opportunities. This is what happened in Japan in



the 1980s and in America in the 1990s. If such a shift in investment occurs, central banks need to raise interest rates. But because inflation was low (and because Austrian economics had long gone out of fashion), the Fed and the Bank of Japan failed to do so. The cost of capital therefore fell below its expected return, fuelling a surge in credit, equity prices and investment.

Investment normally accounts for about one-sixth of America's GDP, but during the three years to 2000 the investment boom pushed up its share of GDP growth to one-third. Overinvestment caused the return on capital to decline. Anybody who looked at the profits of corporate America in 2000, as reported in the national accounts (which allow for the true cost of stock options) rather than by the companies themselves, should have seen trouble coming. Profits had been falling since 1998, as before every previous recession (see chart 2). Investment will not rebound until excess capacity has been

cleared and profits have improved.

Strict Austrian-school disciples would argue that because the current downturn is due to overinvestment, the Fed's repeated easing of interest rates is wrong; it delays the correction of past excesses. The present economic and financial disruption is needed to bring saving and investment back into balance. But most economists today would accept that in the face of a severe recession central banks need to act. Even the Austrian economists recognised that a collapse in confidence could push the economy into a much deeper recession than necessary. Monetary and fiscal policy therefore still has a role—not to avoid recession, but to head off a downward economic spiral.

Many economists still do not accept that this recession has been quite different from all previous post-war cycles, and that the shape of the recovery will therefore also be different. Investment-led downturns tend to last longer because it takes much more time to eliminate financial excesses than to tame inflation. High debts and excess capacity will restrain growth.

The complete rejection of Austrian-school ideas over the past half-century partly reflected a desire by economists to develop a framework that could explain all business cycles. The truth is that there is no single cause of cycles. Sometimes an oil-price shock or a policy mistake may trigger a recession, but the endogenous movements in credit, investment and profits are also always at play. Indeed, the Austrian cycle may become more common again if, as this survey will argue, financial liberalisation has made bubbles in credit and investment more likely. ■

Keeping a lower profile

ECONOMIES are much less volatile than they used to be, for all that the newspaper headlines seem to suggest otherwise. A century ago deep recessions were common; now they are rare. Why has economic activity become less bumpy?

America's NBER has dated the peaks and troughs of the country's cycles back to 1854. Over the years, expansions have got longer and recessions shorter and shallower (see chart 3 overleaf). An analysis by Victor Zarnowitz, an economist at Amer-

ica's Conference Board and one of the world's leading experts on business cycles, has found that before 1945 the American economy was in recession for two years in every five. Since the second world war, it has been in recession only about one year in six, and the average length of a recession has fallen from 21 months to 11. Since 1945 the standard deviation (a measure of volatility) of quarterly changes in GDP has been only half of what it was before 1918 and only one-third of its level in 1919-45.

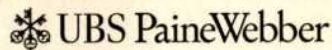
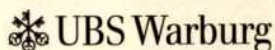
Economies have become less volatile—but they may not stay that way

Other economies have also experienced flatter cycles. An IMF study of 16 developed countries found that the average peak-to-trough decline in GDP during recessions was 4.3% in 1881-1913, 8.1% in the turbulent period between the wars but only 2.3% since 1950.

The business cycle has continued to moderate during the past half-century. In the past 20 years, America has been in recession for only 18 months (assuming the recent one ended in January). Indeed, the ►►



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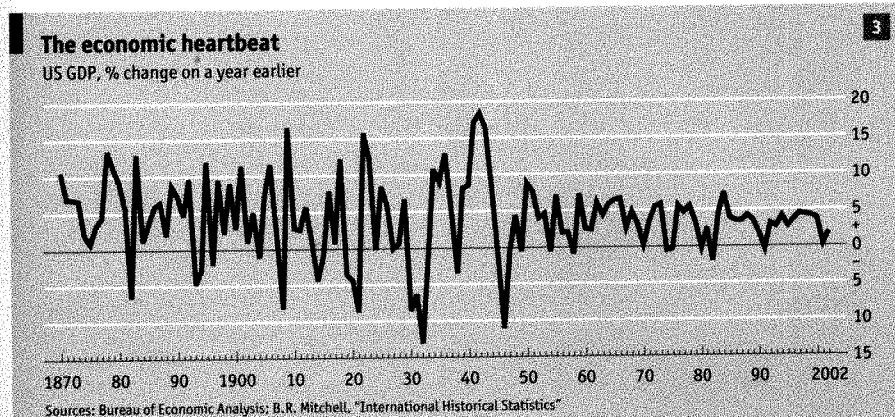


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► past decade was the economy's most stable in its history. An OECD study of 13 developed countries found that economic volatility rose in the 1970s, but has since fallen sharply everywhere. In the 1990s all the big economies were less volatile than in the 1960s—even Japan's (see chart 4).

After 1945, recessions in Japan and continental Europe seemed to disappear. Following the devastation of the war, these economies grew without pause for a couple of decades: Germany did not suffer a fall in GDP until 1967, Japan not until 1974. In general, America's economy has been more volatile than Europe's, with more frequent, though shorter, recessions.

Seeking the source

Economists have plenty of theories about why the business cycle has flattened:

- **Services.** One of the most common explanations involves the shift in output and jobs, first from agriculture to manufacturing and then from manufacturing to services. The variability of harvests makes agriculture the most volatile sector. Services, it is argued, are the least volatile. Households buy durable goods, such as cars, to use over a period of time, so if income falls such purchases can more easily be postponed than services such as haircuts.
- **Better inventory control.** Inventory investment is the smallest component of GDP, but it plays a big role at turning-points in the cycle. Over the past 50 years, changes in inventory investment have, on average, accounted for more than half of the fall in GDP during recessions. But now, thanks to information technology, up-to-the-minute information about sales and inventories and just-in-time production techniques allow firms to hold fewer stocks and to match output more closely to sales. This, it is argued, helps to prevent an unwanted build-up of stocks. American

manufacturers of durable goods now hold only two-thirds as much inventory relative to sales as in the 1970s.

- **Globalisation.** Increasing international trade, the theory goes, operates as a safety valve. During a boom America, say, can tap spare capacity abroad through imports. This helps to hold down prices and so allows the economy to expand for longer without overheating. Conversely, in a recession exports help to offset weak domestic demand.

- **Bigger government.** In recessions governments, unlike firms, do not slash spending and jobs, so they help to stabilise the economy. At the start of the 20th century, public spending amounted to less than 10% of GDP in most countries. Today public spending in developed economies accounts for an average of 37% of GDP. Europe's higher public spending helps to explain why its economies have tended to be more stable than America's.

- **Automatic fiscal stabilisers.** Even more important is the counter-cyclical role played by taxes and unemployment benefits. In a recession, income taxes fall and unemployment benefits automatically rise. This helps to support incomes.

- **Discretionary fiscal policy.** Traditional Keynesians argue that since the Great Depression active measures by governments to cut taxes or increase spending have made recessions less severe. But the effectiveness of fiscal policy is debatable. The stimulus often arrives too late, fuelling tomorrow's boom rather than preventing today's recession.

- **Better monetary policy.** Until the 1930s the money supply typically shrank during recessions, partly because the gold standard denied countries any independent monetary policy. This caused deflation, and by increasing the real burden of debt deepened recessions. According to the

IMF, before the second world war two-fifths of recessions were accompanied by falling consumer prices. Since then, only Japan has experienced deflation. At the other extreme, rising inflation in the 1970s exacerbated economic volatility because it forced central banks to slam on the brakes. Since the 1980s, more prudent monetary policy has helped to stabilise output.

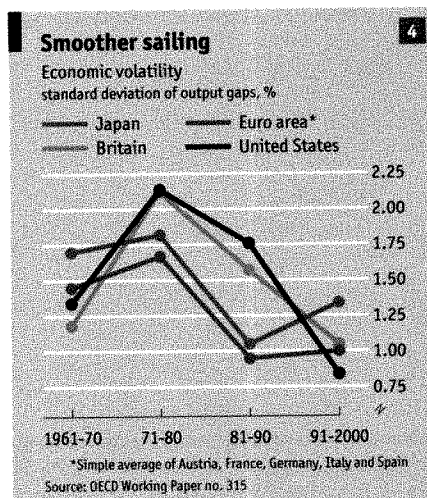
- **Bank reform.** Some of the worst recessions before the second world war were aggravated by banking crises. The introduction of deposit insurance, bank supervision and regulation, and a stronger lender-of-last-resort role for central banks has helped to prevent the panics that could turn recessions into depressions.

- **Financial deregulation.** The improved efficiency of financial markets in recent years has made it easier for consumers and firms to smooth their spending over time. Better access to consumer credit has allowed households to go on spending even if their incomes drop temporarily.

Taking stock

With so many reasons for greater stability, it is a wonder that the business cycle has any pulse left at all. But which of these reasons really matter? If volatility has lessened because of structural changes, such as the shift to services or new technology, then the change may be permanent. If, as others claim, milder recessions largely reflect better monetary policy, or a large dose of good luck, then the flatter cycles will persist only for as long as good policy or good luck continues.

Probably the two most important reasons why recessions have become milder since the second world war are higher government spending and hence more pow- ►►



erful built-in fiscal stabilisers, and measures to prevent banking crises. Neither of these is likely to be fundamentally reversed. But there is less agreement about the reasons for the decline in economic variability over more recent decades. Several of the explanations that hinge on structural changes do not stand up to scrutiny.

Take the shift from manufacturing to services. Services have increased from 39% of America's GDP in 1960 to 55% in 2001. But if the relative weight of manufacturing and services had remained constant over those 40 years, the decline in economic volatility would have been virtually the same. Many services, from telecommunications and air travel to finance and advertising, are in fact highly cyclical.

The idea that globalisation can cushion downturns is also suspect. If anything, increased global integration exacerbated the recent downturn, as most of the world slowed in unison. As American firms slashed their IT spending, they pushed East Asia into recession. Those economies, in turn, cut their imports from America, deepening the initial downturn.

Better inventory control as an explanation for reduced volatility has also lost some of its appeal. In the fourth quarter of 2001 American firms slashed their inventories by the equivalent of more than 3% of output, the biggest reduction in over 50 years. At first sight, this suggests that for all their investment in IT, firms are still not managing their inventories effectively. A study by James Kahn and Margaret McConnell, two economists at the New York Fed, concludes that during most of last year's recession firms did manage their stocks better than in previous post-war cycles, but that in the fourth quarter of last year firms were caught out by an unexpected rise in demand as consumers took advantage of free credit, so they had to run down inventories. IT allows firms to adjust output more rapidly to changes in sales, but it has not solved the problem of forecasting demand.

A study by Olivier Blanchard, at MIT, and John Simon, at the Reserve Bank of Australia, concludes that much of the dampening of the economic cycle in the big economies is due to a decline in inflation volatility (on top of the fall in inflation itself). The volatility of inflation increased in the 1970s, at the same time as output volatility, and then fell from the mid-1980s onwards as central banks were given more independence to pursue price stability. By anchoring inflationary expectations, central banks have made economies more sta-



ble. Unlike other theories, this explains why economic instability increased in the 1970s and then declined.

James Stock, at Harvard, and Mark Watson, at Princeton, agree that better monetary policy has been an important factor. They estimate that it could account for up to a quarter of the total reduction in the volatility of America's GDP in the 1990s. They rule out better inventory management as an important cause of lessened volatility. A large part of the fall in output volatility seems to be due to a fall in the volatility of sales rather than to an improved match between production and sales. Another quarter of the decline in volatility seems to be due to the fact that there were fewer external shocks, such as jumps in oil prices. But the two economists reckon that sheer luck explains as much as half of the fall in volatility in the 1990s. In other words, it cannot be relied upon to continue indefinitely.

One important element of good luck in the 1990s was that the big economies became unusually decoupled, in contrast to the 1970s and 1980s when they were more synchronised. When different economies boom together, inflation is likely to pick up sooner and so bring the expansion to a halt. But in the 1990s the big economies were mostly out of step. When America fell into recession in 1990 the economies of Japan and continental Europe remained robust, helping to cushion America's downturn. Europe was given a boost by German unification, and Japan's economy remained bubbly until 1992. Only after America's recovery was well under way did Japan and continental Europe stumble.

During America's boom, European

growth was restrained by tighter fiscal policies in preparation for monetary union, and Japan stagnated. Weak overseas demand helped to hold down America's inflation, allowing its boom to continue for longer than usual. Later in the decade, the spare capacity caused by the slump in East Asia also helped to restrain inflation. But this decoupling was a fluke. If economies become more synchronised again, volatility is likely to return.

The reluctant recession

Whatever the reasons for the flatter business cycles over the past couple of decades, the mildness of America's recent recession is still surprising. Despite a stockmarket slump, the bursting of the IT investment bubble, a jump in oil prices and the tragic events of September 11th, the recession was one of the mildest on record. From peak to trough, GDP fell by only 0.6%, compared with an average decline of just over 2% in recessions since the second world war.

One possible explanation is that because America's trend rate of growth has risen, thanks to faster productivity growth, an absolute drop in output becomes less likely when the economy slows. Most economists reckon that America's potential growth rate is now 3.3.5%, compared with 2.7% in 1980-95. This means that if growth falls by three percentage points below trend the economy now simply stalls, whereas previously it would have contracted.

Monetary and fiscal easing played a big part in keeping the recession in check. Interest rates had been cut by three percentage points even before September 11th, to be followed by almost two more points afterwards—the biggest reduction in two decades. And by sheer luck, the tax cuts, planned when the economy looked stronger, turned out to be particularly well timed, as did the increase in government spending in the wake of September 11th.

Another element of luck was that America entered the recession without the over-supply of housing that has been the norm in previous downturns, because builders had underestimated the extra demand resulting from immigration. Combined with low interest rates, this has fuelled a housing boom, helping to shore up consumer spending.

The increased efficiency and resilience of financial markets also deserves some credit. American banks entered the recession with strong balance sheets. More important, the capital markets provided a ▶▶

ready alternative supply of credit through last year's downturn. The financial sector, it is argued, helped to insulate the economy from the financial implications of the recession by redistributing risk. A large chunk of bank lending during the boom had been bundled into securities and sold on the secondary market, shifting risk away from banks to institutions better able to bear it.

A final explanation for America's surprisingly mild recession, favoured by Alan Greenspan, is the increased flexibility of

business, thanks in part to its use of IT. More nimble firms with better information are able to adjust more quickly. Flexible labour and product markets also allow economies to cope with shocks more effectively. This may explain why recessions often last longer in Europe's set-in-their-way economies. In Germany, recessions since 1960 have on average lasted almost twice as long as in the United States. Because of market rigidities, economic excesses take longer to wring out.

Economies may be less bumpy than

they used to be, but until somebody invents an antidote to swings in the mood of firms, investors and consumers, cyclical fluctuations will persist. The mildness of the recent recession and the decline in economic volatility over the past decade were both partly due to luck. In a later chapter this survey will argue that the economic cycle could become more volatile as the luck of the 1990s fades, and booms and busts in asset prices occur more often. What can fiscal and monetary policy do to cushion the ride? ■

Weapons of mass distraction

Can monetary and fiscal policy eliminate the business cycle?

THE ability of macroeconomic policy to erase the business cycle has in turn been greatly over- and underestimated over the decades. The broad consensus now is that monetary and fiscal policy can moderate the ups and downs, but they will never abolish the cycle altogether.

In the 1950s and 1960s policymakers believed that by increasing government spending, trimming taxes or cutting interest rates they could avert recessions and control unemployment. But as inflation took off in the 1970s and public debt exploded, Keynesian fine-tuning went out of fashion. Policy in the 1980s and 1990s was aimed largely at reducing inflation, not stabilising output. Governments rejected active monetary and fiscal policies in favour of adherence to rules. Central banks were made independent, and many were given explicit inflation targets. Meanwhile, governments laced themselves into fiscal straitjackets. America set balanced-budget targets in the 1990s and the euro area adopted a fiscal stability pact with strict limits on government borrowing. The notable exception was Japan, which embarked on a decade of fiscal expansion.

In the past year, interest in fiscal policy has revived. The American government administered its biggest budget stimulus for two decades. In the euro area, too, there has been a vigorous debate about whether governments should stick to their medium-term fiscal targets or allow budget deficits to widen as their economies weaken. So why did governments abandon fiscal policy in the first place?

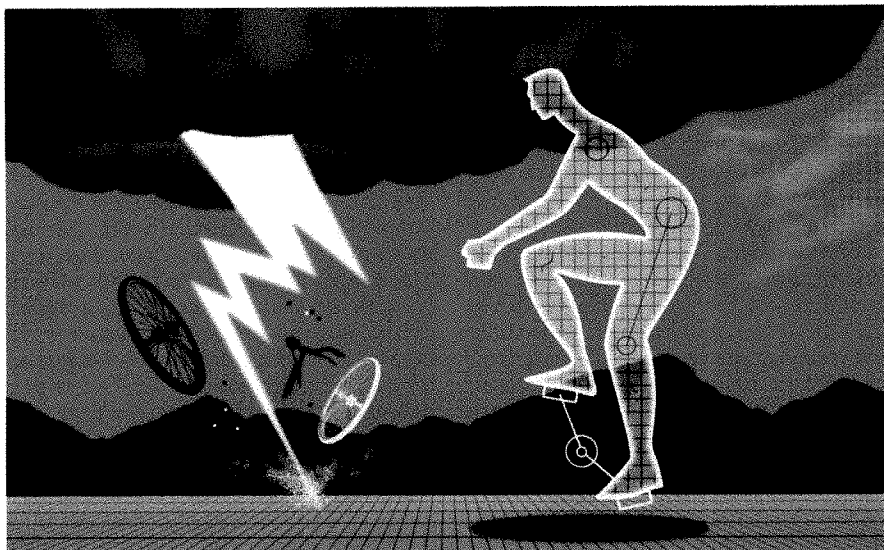
The first reason was that public debts were on an unsustainable path. But after a

decade of fiscal rectitude, by 2000 budgets in most rich countries had moved close to balance, if not surplus. That allows governments to have a more flexible fiscal policy. A second reason for disenchantment with fiscal measures was a widespread conviction that they did not work. Extra government borrowing, the argument went, would push up long-term interest rates and crowd out private investment. In addition, as public debts mount up, households expect taxes to rise in future so they may save more, offsetting the stimulus—the so-called “Ricardian equivalence” effect. In practice, most studies have found that an increase in government borrowing does indeed boost demand. However, recent research suggests that fiscal policy

may pack a smaller punch than it used to.

Roberto Perotti, an economist at the European University Institute in Florence, examined fiscal policy in five countries (America, Britain, Canada, Germany and Australia) and estimated the impact on GDP of discretionary fiscal-policy changes after stripping out the automatic movements in taxes and spending over the cycle. He found that the effects of fiscal policy on GDP have become much weaker in the past 20 years compared with the previous 20. Also, increases in public spending have less effect on demand in smaller economies than they do in America.

Identifying the size and impact of discretionary fiscal policy is a tricky business, so it would be unwise to place too much



weight on the exact size of the fiscal impact estimated by Mr Perotti. But the evidence that fiscal policy is becoming less effective is worth bearing in mind. This does not seem to be due to a change in monetary policy. Mr Perotti finds that real interest rates increased by less in response to bigger budget deficits in the later two decades than in the first. Nor can it be explained by households saving more for fear that unsustainable public debts will force governments to raise future taxes: personal saving rates have fallen over the past two decades in most economies.

One possible explanation lies in the increased openness of economies and greater international capital mobility. This means that a larger share of any increase in spending leaks into imports, and that a fiscal stimulus may be offset by a stronger exchange rate as higher bond yields attract capital inflows. A recent IMF paper on the impact of fiscal policy during recessions in 29 countries since 1970 found that in relatively closed economies (where imports

amounted to less than 20% of GDP), such as America and Japan, fiscal policy did boost output during recessions, although by less than generally assumed. But in open economies with floating exchange rates a fiscal stimulus had little effect.

Even where fiscal policy still works, getting the timing right is tricky. In some countries, notably the United States, it can take months to get political approval. By the time a stimulus is administered, the economy may have already recovered. In contrast, interest rates can be cut without delay, and swiftly reversed if the economic outlook suddenly improves.

Discretionary budget measures are therefore usually best avoided. Built-in fiscal stabilisers may be more effective. The automatic fall in taxes and rise in jobless benefits in recessions help to support spending. An OECD study estimates that in the 1990s automatic fiscal stabilisers on average reduced cyclical fluctuations in rich economies by a quarter. In countries with large government sectors, such as Fin-

land and Denmark, they reduced output volatility by more than half; in Japan and America, where taxes and spending are smaller relative to GDP, their effect was more modest. A study by Alan Auerbach, at the University of California, Berkeley, finds that in America fiscal stabilisers remain just as potent today as in the 1960s.

Ideally, budget deficits should be broadly balanced over the cycle, but automatic fiscal stabilisers should be allowed to take full effect. There is nothing wrong with a budget deficit in a recession, so long as it moves into surplus during the boom. In the euro area an individual country cannot cut interest rates to counteract a shock that affects only its own economy, so allowing automatic fiscal stabilisers to operate is especially important.

Europe's stability pact is too rigid. It sets a limit of 3% of GDP on budget deficits and requires budgets to be balanced in the medium term. That does not leave enough room for budget deficits to widen in a recession. Portugal broke the 3% ceiling last

Crystal balls-up

"Forecasting is always difficult, especially when it is about the future"

THE dismal scientists have a dismal record in predicting recessions. In 1929 the Harvard Economic Society reassured its subscribers days after the crash that: "A severe depression is outside the range of probability." Despite huge improvements in data and computing power, forecasters remain in the dark. In a survey in March 2001, 95% of American economists thought there would not be a recession, yet one had already started.

Why are recessions so difficult to forecast? One excuse is that economists, unlike weathermen, do not know if it is hot or cold today because their data are always out of date. They have to forecast not only the future but also the immediate past. A less good reason is that economists have a tendency to run with the pack. Predicting a recession is unpopular (especially if you work for an investment bank), and predicting one prematurely will prove costly to clients. It may also cost you your job.

Forecasts produced by economic models with hundreds of equations are notoriously bad at predicting recessions

because they tend to extrapolate the recent past. This leads to big forecasting errors near turning-points, because recessions are caused by abrupt changes in the behaviour of firms and consumers. A more reliable way to spot a coming downturn is to scrutinise indicators that have given warning signals in the past. Financial indicators have the longest lead times, but a gauge that performs well in one period may do badly in another. An inverted yield curve (meaning that short-term interest rates have risen above long-term rates) has traditionally been one of the best predictors of recession. But ahead of America's 1990-91 recession the yield curve did not properly invert.

Stockmarkets are another favourite bellwether. But Paul Samuelson, a Nobel prize-winner in economics, famously quipped that the market had predicted nine of the past five recessions. In 1987, for instance, the stockmarket wrongly signalled a recession in America and Europe. Few economists believe that the recent market slide signals a further recession.

Leading indicators that combine sev-

eral economic and financial measures seem more promising. The index of leading economic indicators (LEI), originally produced by America's Department of Commerce and now by the privately run Conference Board, is a weighted average of indicators such as share prices, interest-rate spreads, consumer confidence and new orders. Unfortunately, the LEI failed to predict any of the past three recessions.

The Economic Cycle Research Institute, a private research group, has been more successful. It was set up by the late Geoffrey Moore, a pioneer of research into business cycles. ECRI believes that turning-points can be systematically predicted. It tracks no fewer than 14 leading indices for different parts of the economy and with different lead times. ECRI was one of the few firms to forecast both of the past two American recessions. Its leading indicators for other economies have also fared well. It successfully forecast recessions in Japan in 1997 and 2001. Encouragingly, as this survey went to press ECRI was saying there was no risk of a double dip in America.

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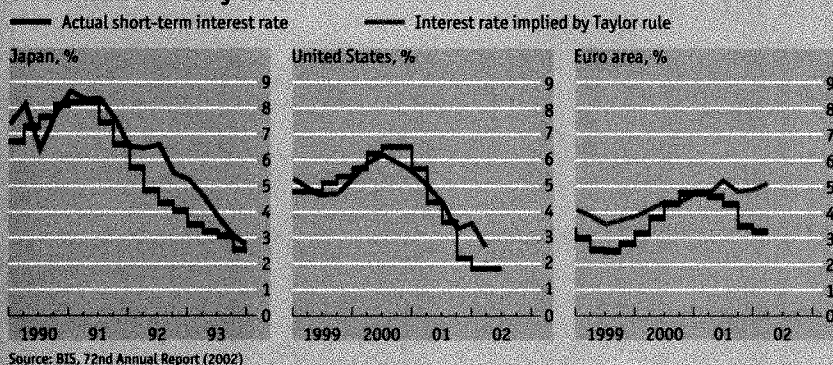


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On the same monetary track



year and is now having to tighten its fiscal policy severely, despite weak growth. Germany also seems almost certain to bust the 3% ceiling this year.

Given the difficulty of timing a fiscal stimulus correctly, most economists agree that monetary policy is a better tool for stabilising growth. Yet how does this fit with the widely held view that central banks' prime goal should be price stability? According to Ernst Welteke, the president of the German Bundesbank, "The European Central Bank doesn't have the job of steering the economy. The best contribution monetary policy can make to growth and employment is to keep prices stable."

Inflation isn't everything

In practice, however, central bankers do not concentrate on inflation to the exclusion of everything else. Benjamin Friedman, an economist at Harvard University, argues that although central bankers strenuously deny having any policy objective other than price stability, in practice they all take growth into account. For example, if inflation rises above target, a central bank will generally aim to reduce it gradually rather than suddenly, to avoid inflicting too much damage on growth.

Besides, by aiming to keep inflation stable a central bank will, in effect, also stabilise output. When the economy is producing below potential, inflation will fall and the central bank will cut interest rates, helping to boost growth. When output is above potential, inflation will rise and the central bank will increase interest rates, thereby dampening down growth.

The popular perception is that America's Fed takes more account of growth than the ECB. Whereas the Fed often explains its interest-rate cuts in terms of proping up demand, the ECB always puts inflation first. Yet an analysis by the Bank for

International Settlements (BIS) suggests that differences between the two central banks' policies are much exaggerated.

Chart 5 compares actual interest rates with those that would be required under the "Taylor rule". Named after its inventor, John Taylor, now at America's Treasury, this offers a method of calculating the appropriate interest rate, taking into account the difference between actual and target inflation and the size of the output gap (the amount by which actual output is above or below potential output).

The chart shows that, allowing for different movements in output and inflation in each economy, the Fed and the ECB seem to set interest rates in fairly similar ways. The ECB cut interest rates by less than the Fed last year because the economic slowdown in Europe was less severe than in America and because inflation was higher. The BIS's chart also shows that, judged by the Taylor rule, the Bank of Japan cut interest rates just as fast after Japan's bubble burst in the early 1990s as the Fed did last year.

In recent years Americans have placed excessive faith in the ability of the Fed, and particularly of Alan Greenspan, to tame the economic cycle. But monetary policy cannot be used with surgical precision. Not only are there long and variable lags before changes in interest rates affect output, but there is also much uncertainty about the potential growth rate and the size of the output gap.

Many people believe that the sharp increase in inflation in the 1970s could have been avoided if only the Fed had been using today's monetary-policy framework. But work by Athanasios Orphanides, an economist at the Fed, suggests that if the central bank had used the Taylor rule, inflation in the 1970s would have been just as high. It was not the monetary frame-

work that caused inflation to surge, he argues, but a misperception of the size of the output gap. Official estimates of potential output at the time failed to spot the slowdown in productivity growth in the late 1960s and early 1970s. Partly as a result, monetary policy tried to stabilise output at too high a level, causing inflation to rise.

In 1973 the output gap was estimated at minus 3%, implying considerable economic slack. With the benefit of hindsight, it is now put at plus 4% for that period, implying massive upward pressure on inflation (see chart 6). With such measurement errors, a monetary policy that tries too hard to smooth the cycle could easily increase output volatility.

Too low for comfort

Nevertheless, compared with the double-digit inflation rates in the 1970s, low and less volatile inflation has helped to deliver greater economic stability. In many economies inflation is at its lowest for 40 years. Might it now be too low?

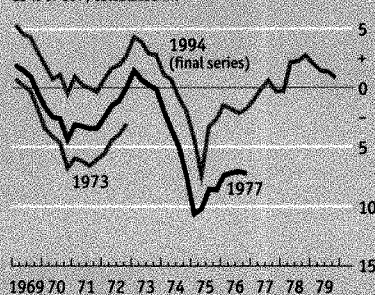
Once inflation is around 3%, squeezing it even lower will do little to improve an economy's growth performance. Indeed, as inflation approaches zero, the risks of greater economic volatility start to rise. One reason is that interest rates cannot be negative, so if inflation is close to zero there is no way to achieve the negative real interest rates that may be needed to stimulate an economy. This is the so-called "liquidity trap" into which Japan has fallen.

If real interest rates are too high, the risk of deflation increases. Deflation is much more damaging to economic stability than inflation. It deepens recessions because it increases the real burden of debt and encourages consumers to delay purchases in the hope of even lower prices later.

The lower the average inflation rate, the ➤

Mind the gap

Official estimates of America's output gap* as % of GDP, calculated in:



*Actual GDP minus potential GDP
Source: Athanasios Orphanides, ECB Working Paper no. 15

greater the risk of falling into the liquidity trap. Simulations by the IMF conclude that given the range of economic shocks experienced over the past 40 years, the probability of interest rates hitting zero—and hence the risk of deflation—increases markedly if average inflation targets are set below 2%. Moreover, as inflation falls below 2%, the volatility of output starts to increase. This suggests that the mid-point of an inflation target should be set well above 2%. The Bank of England and the Reserve Bank of Australia both have mid-points of 2.5%, but the ECB's target is "less than 2%", which is far too strict. If central banks set their inflation sights too low, warns Olivier Blanchard at MIT, at some point in the next decade another country is likely to

join Japan in a liquidity trap.

That fate may yet befall the United States. Its inflation rate, measured by the GDP deflator, is currently running at only 1%. If America's recession were to resume, the Fed's ability to act would be limited.

The bank seems to be well aware of this risk. In a recent Fed study of Japanese deflation, it argues that monetary policy in Japan in the early 1990s was not too tight, given the forecasts of growth and inflation at the time, and fiscal policy was generally expansionary. However, growth and inflation forecasts consistently proved too high. At the time, nobody in Japan or abroad was predicting deflation. The Bank of Japan's big mistake was to fail to take out the necessary insurance against downside

risks when its bubble had burst.

The Fed concludes that as interest rates and inflation move closer to zero and the risk of deflation rises, central banks need to cut interest rates by more than would normally be justified by prevailing economic conditions. Once deflation emerges, monetary policy can do little to pull the economy out of a slump. If, on the other hand, a central bank injects too much stimulus, it can correct this later.

Keynes argued that even when deflation has taken hold and monetary policy is "pushing on a string", fiscal policy can still stimulate demand. Japan has tried this, running a huge budget deficit over the past decade, yet its economy remains sick and prices continue to fall. Why? ■

Japan's lost decade

Japan is not so much in a cycle as in a rut

THE annual growth rate in Japan has averaged less than 1% over the past ten years, compared with over 4% in the previous decade. The OECD estimates that Japan's output gap, a measure of spare capacity, is a modest 3% of GDP, but this assumes that its potential growth rate has fallen sharply along with its actual growth. If productivity growth had remained constant at its 1980-92 average, then Japan's output gap would now be a huge 18% of GDP (see chart 7). Assuming that the truth lies somewhere in-between, Japan has suffered the deepest slump in any developed economy since the Great Depression.

Japan's policymakers, unlike America's in the 1930s, appear to have followed the Keynesian textbook: the government's budget has swung from a surplus of 2% of GDP in 1990 to a deficit of 8% of GDP. Yet the economy is still flat on its back. Is this more evidence, as argued in the previous section, that fiscal policy is becoming less effective? Some economists conclude that fiscal policy simply does not work in Japan. The government's debt of 140% of GDP is unsustainable, especially considering the future burden of a rapidly ageing population. Households know that taxes will need to rise, it is argued, so they save more, neutralising the fiscal stimulus.

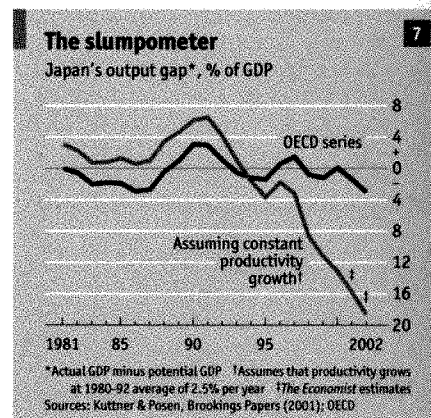
Kenneth Kuttner, of the New York Fed, and Adam Posen, of the Institute for International Economics, disagree. They argue that fiscal stimuli in Japan in the past de-

cade have been successful in boosting demand. Without them, Japan's economy would have been even weaker. However, the government's fiscal stimulus has been more modest than generally thought. The endless packages announced by the government did not contain as much new money as they appeared to. Most of the increase in the budget deficit has been caused not by public-spending increases or tax cuts, but because tax revenue has automatically shrunk as output has fallen.

Watch that output gap

Widely quoted OECD figures show a big increase in Japan's structural budget deficit during the 1990s. But if, as suggested above, Japan's output gap is really much bigger than the OECD estimates, the discretionary fiscal stimulus must have been smaller. Messrs Kuttner and Posen reckon that since 1997 fiscal policy has been causing output to contract. But in earlier years, when there were genuine tax cuts or spending increases, they did boost GDP.

Far from being ineffective in Japan, fiscal policy might actually work better there than in some other countries, because Japan is relatively closed to international trade and capital. Imports account for only 10% of GDP, the lowest proportion in any OECD country, and capital is still not fully mobile: Japanese savers remain reluctant to move their money abroad in search of higher returns. This captive pool of saving



makes it easier to finance debt without pushing up interest rates.

The alarming increase in Japan's public debt has prompted talk in Tokyo about cutting government borrowing. Now is not the time. A rise in taxes would reduce growth and hence tax revenues, thereby increasing the government's deficit even further. Mr Posen argues that even now it is neither too late nor too costly for Japan to revive its economy by pursuing proper fiscal reflection, financed by the Bank of Japan buying government bonds.

But the shape of any fiscal stimulus is as important as its size. Japan's earlier packages were never designed for maximum macroeconomic effect, but often to help out politically well-connected firms. Dur-

ing the past decade, tax cuts have done much more to stimulate demand than increases in public spending, partly because public works were widely regarded as wasteful. This suggests that a reduction in public works accompanied by an identical cut in taxes would boost GDP.

Martin Feldstein, the president of America's NBER, suggests the use of targeted fiscal incentives. For example, the government could announce that the rate of sales tax was to be cut immediately from 5% to zero for a limited period, after which it would increase gradually to 10% once the economy was growing again. That would give consumers an incentive to buy goods now. It would, in effect, offset deflation, by creating an expectation of rising prices. The immediate revenue loss could be made up by cutting public works, and the future tax increase would put Japan's finances on a sounder path.

Demand or supply?

Some economists think this emphasis on boosting demand is misplaced. Echoing the Austrian economists, they argue that monetary and fiscal stimulus is a narcotic that prevents structural adjustments. Japan's real problem, they say, is the failure of the government to clean up the banking system. Banks keep rolling over bad loans rather than writing them off. This sustains overcapacity as unprofitable firms are kept alive, and locks resources into low-return



sectors such as construction and retailing.

In a provocative paper, Robert Dugger and Angel Ubide, economists at Tudor Investments, an American fund-management company, argue that Japan is not in a "liquidity trap" but a "structural trap", meaning that political and economic obstacles are preventing the reallocation of capital from low-return to higher-return firms. The symptoms—slow growth and deflation—are the same as those of a liquidity trap, but the condition calls for a different policy response.

In a structural trap, loose monetary and fiscal policy can exacerbate deflation and sluggish growth because unproductive but politically important firms are allowed to

survive. In Japan public works have propped up inefficient construction firms; subsidies and zero interest rates help troubled firms to stay in business. By perpetuating excess capacity, this feeds deflation.

Messrs Dugger and Ubide argue that if there is strong political resistance to reallocating capital, as in Japan, monetary policy needs to be tighter than if the government were actively attacking the economy's structural rigidities. Higher interest rates, they argue, would force unprofitable firms out of business, eliminate excess capacity and release labour and capital for more productive uses.

However, raising interest rates to eliminate inefficient firms goes well beyond the mandate of any central bank. Moreover, although scrapping excess capacity would improve the return on capital and eventually help to boost growth, in the short term it would worsen deflation as unemployment rose. Much better that the government should clean up the banking sector, forcing banks to write off bad loans, which would cause unprofitable firms to close down. Monetary and fiscal policy could then be used to cushion, not prevent, the painful consequences.

Market rigidities may well blunt the effectiveness of monetary and fiscal policies. For Japan, macroeconomic stimulus and microeconomic reforms are not alternatives: they should be used to complement each other. ■

A necessary evil

WHEN America's bubble burst last year, the Fed swiftly cut interest rates. This has become a habit: every time there has been any financial turmoil at home or abroad—such as the crises in East Asia and Russia and the near-collapse of Long Term Capital Management in 1998—the Fed has pumped more money into the economy. Low interest rates have saved America from a deep recession. But after such a binge, might the economy not benefit from a cold shower?

Most people would consider this a heretical question. They assume that it is a central bank's job to avoid recessions at all cost. According to one survey, four-fifths of Americans believe that preventing recessions is as important as preventing drug

abuse. But are recessions always an unmitigated disaster, or do they also offer some economic benefits? And if central banks respond to every danger sign by pumping in more money, does this not risk simply transferring the problem elsewhere? As America's stockmarket bubble has burst, another bubble now seems to be inflating in its housing market. This allows consumers to go on partying, but what happens when the drink runs out?

According to the Austrian economic paradigm described in the second section of this survey, recessions are a natural feature of an economy. Joseph Schumpeter argued that recessions are not an evil that should be avoided, but a necessary adjustment to change. Only by allowing the

Should we learn to love recessions?

"winds of creative destruction" to blow freely could capital be released from dying firms to new sectors of the economy, thereby boosting future productivity.

Hayek counselled against massive monetary easing to prevent a recession. If unprofitable investments were made during a boom, then it was better to shut those firms down and clear the way for new, more productive investment. For the Austrian economists the policy choice is not between recession or no recession, but between one now or an even nastier one later. A recession is necessary to work off an imbalance between too much investment and too little saving.

Keynes, quite reasonably, ridiculed the idea that in the long run the Great Depres-

► sion might turn out to have been a good thing. In the early 1930s the Fed and the American Treasury did not pursue expansionary policies, precisely because they thought these might hinder the necessary adjustment. Andrew Mellon, the secretary of the Treasury, urged the market to "liquidate labour, liquidate stocks, liquidate the farmers, and liquidate real estate...It will purge the rottenness out of the system." America's output duly fell by 30% as the Fed sat on its hands.

Today, a slump on that scale would be unlikely even if the Fed had not cut interest rates swiftly. It would have been headed off by a variety of changes made since the Great Depression: higher government spending and hence more powerful automatic fiscal stabilisers; bank deposit insurance; and a stronger commitment by the Fed to its role of lender of last resort. But even the Austrian economists themselves came to reject the idea that faced with a potentially severe recession, policymakers should do nothing. They approved of stimulus measures to stop recessions from turning into deep depressions, but not of preventing recessions altogether.

The case for the defence

Why is economic instability always assumed to be bad? Some economists argue that recessions result in a permanent loss of output. This rests on the notion that there is a fixed ceiling for output, rising over time, so any shortfall against potential is a permanent loss. On this view, demand-management policies can fill in the troughs without shaving off the peaks, thus increasing average growth.

A more realistic way of looking at it, however, is that business cycles are fluctuations in output above and below an equilibrium trend. This suggests that demand-management policies can mitigate recessions only to the extent that they also choke off expansions; they cannot increase the average rate of growth or employment. Admittedly, cyclical increases in unemployment may become permanent if labour-market rigidities, such as strict hiring-and-firing laws, make it hard for the jobless to find work even when the economy recovers, a condition known as hysteresis. If this is present, as it is in many European countries, then recessions can have a permanent cost. But this is really an argument for labour-market reform to minimise the cost of recessions, not one for measures to prevent them altogether.

A second argument against letting recessions rip is that households may value



economic stability for its own sake, even if it makes no difference to the average unemployment rate. Justin Wolfers, an economist at Stanford University, has used surveys of consumer satisfaction from several rich economies to estimate the value that households place on stability. He reckons that starting from current levels of volatility, eliminating the business cycle would increase average well-being by the equivalent of a fall in the unemployment rate of only 0.2 percentage points. By contrast, labour-market reforms could reduce unemployment by several percentage points.

A third common claim is that economic instability and uncertainty may discourage investment, thereby reducing long-term growth. Yet the evidence is weak. More volatile economies do not appear to invest less as a share of GDP. Moreover, looking back, the 20 years to 1938 were by far the most volatile in economic history, yet the average growth rate in developed economies was 3.8%, well above the average growth of 2.7% during the past two decades of relative stability. An analysis of 20 developed economies since 1960 by Bill Martin of UBS Global Asset Management finds little evidence that macroeconomic stability promotes faster growth. If anything, he concludes, countries with greater output variability have enjoyed slightly faster growth in productivity.

This is not as odd as it sounds. A perfectly stable economy would miss out on the advantages of booms as well as the alleged disadvantages of slumps. For instance, in boom times, when credit flows freely, it is easier to finance the risky innovations that may boost future productivity growth. Booms also encourage mergers and acquisitions, a powerful tool for restructuring. More important, as Schumpeter argued, recessions are a process of creative destruction in which inefficient firms are weeded out, releasing resources for

more productive firms.

But can we be sure that it will be the least productive firms that go bust in recessions, and that they really will be replaced by new, more profitable ones? Awkwardly, work by Ricardo Caballero and Mohamad Hammour, economists respectively at MIT and DELTA, a French research organisation, finds that good times may be more conducive to economic restructuring than bad. The two economists examined gross job creation and destruction in American manufacturing over the period 1972-93 and found that at the onset of a recession job destruction increases, but it then falls below normal levels until well into the recovery. Job creation declines during a recession and remains relatively low during the initial recovery. Adding up the net effect of job destruction and creation, Messrs Caballero and Hammour conclude that the pace of restructuring actually falls during a recession.

The figures on which the study was based are available only for manufacturing, which has a shrinking share of the economy. Once services are added in, the picture might look different. Still, the study does raise the question of why recessions might hinder rather than help industrial restructuring. One answer is that credit markets are imperfect. When credit is tight in a recession, even profitable firms can find it harder to raise money to finance restructuring or new investment.

The dark side of the boom

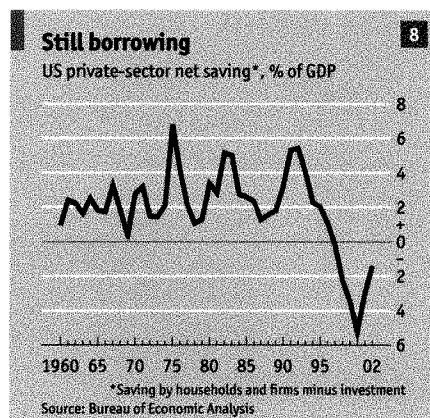
Even if recessions are not always the most efficient way to reallocate resources, they are necessary to purge the excesses of the previous boom. Stephen King at HSBC argues that a recession should be seen as an unpleasant cleansing experience which leaves the economy in a healthier state: "A bit like taking a cold shower with a lump of carbolice soap." But America's economy ►

has not yet completed this cleansing process: it still has an inadequate savings rate, excessive debt and a huge current-account deficit. The recent mild recession did little to correct these imbalances, making further pain inevitable.

A good indication of the size of the adjustment yet to be made is the private sector's financial balance (or private-sector net saving, equivalent to saving minus investment), a concept elaborated by Wynne Godley, an economist at Cambridge University. In the United States the private-sector balance shifted from a surplus of 5% of GDP in 1992 to a deficit of 5% of GDP in 2000 as households and firms went on a borrowing spree, an astonishing change after almost four decades when the private sector never ran a deficit at all (see chart 8).

The corporate sector's financial position was not wildly out of line with previous periods of expansion: firms usually run a deficit during booms to finance investment. It was the behaviour of the personal sector that was exceptional, and remains so. The surge in share prices during the 1990s encouraged households to save less and less.

In the past, when a country's private-sector net saving has fallen so sharply, a deep recession or a prolonged period of



stagnation has usually followed. Events in Japan, Britain and Sweden after their late 1980s booms are prime examples. Mr Godley has long argued that the same outcome is inevitable in the United States. But America's adjustment still has a long way to go. The private sector's financial deficit has narrowed to 1.4% of GDP this year, but that still leaves it well below its 1960-95 average of a surplus of 3% of GDP.

So far, most of the belt-tightening has come from firms, which have slashed their investment and laid off workers. Consumers, on the other hand, have continued to

borrow, encouraged by easy money and rising house prices. But the collapse in share prices is now likely to prompt households to save more of their income. If the household saving rate rises back to its long-term norm, at the very least a period of slow growth, and perhaps another recession, will surely follow.

Was it a mistake for the Fed to slash interest rates last year and thereby delay this adjustment by households? Some economists believe that a deep but short recession is preferable to a prolonged period of sluggish growth, because recovery comes much sooner, with less damage to the economy's potential growth rate. However, it is arguably better to unwind imbalances gradually to avoid the risk of severe financial problems. Moreover, the Fed has been worried that a deeper recession at a time when inflation is already so low might lead to debt deflation, which central banks should avoid like the plague.

Lower interest rates have helped to prop up spending in America largely by fuelling a credit-driven boom in house prices. This fixes one problem at the risk of creating another. Rather than injecting more liquidity, would it not be better if central banks tried to smooth the path of credit over the whole business cycle? ■

Bubble and squeak

AMERICA'S current economic woes—from the collapse in share prices to the surge in bankruptcies—can all be traced back to the biggest credit boom in its financial history. Private-sector credit surged at an unprecedented pace in the late 1990s (see chart 9). Without easy credit the stock-market bubble could not have been sustained for so long, nor would its bursting have had such serious consequences. And unless central bankers learn their lesson, it will happen again.

Central banks' main task over the past two decades has been to defeat inflation. But now they face an even tougher challenge: preventing ever bigger booms and busts in economic activity caused by increasingly large swings in asset prices and credit. Low and stable inflation was supposed to promote financial stability, yet greater stability in inflation and output has not been reflected in greater asset-price

stability. Instead, the prices of assets, such as shares and property, have been subject to bigger swings over the past two decades. It now seems clear that low inflation does not guarantee financial stability. The three biggest bubbles this century—America's in the 1920s and 1990s and Japan's in the 1980s—all developed when inflation was low.

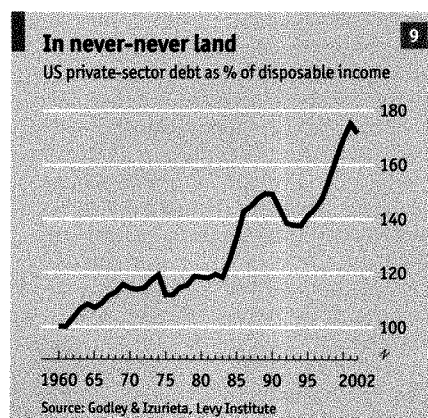
Indeed, low inflation may even encourage a build-up of financial imbalances. It can heighten the excessive optimism that helps to fuel unsustainable booms in credit and asset prices. If people believe that central banks are fully committed to price stability, inflation will be held down even as demand pressures mount, removing the need to raise interest rates sharply. That encourages a bigger build-up of debt and higher share prices as firms and households come to believe that the expansion will continue indefinitely—as

they did in America in the 1990s.

Central banks need to keep a closer eye on credit and asset prices

they did in America in the 1990s.

A paper by Claudio Borio and Philip Lowe, economists at the BIS, suggests that a useful way of gauging the vulnerability of a monetary regime to financial instabil-



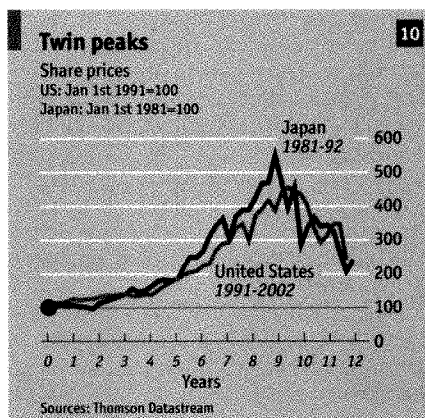
ity is to consider its "elasticity": its potential to allow financial imbalances to build up unchecked during a boom. Compared with the early part of the 20th century, today's financial regulation and supervision helps to curb banks' ability to lend recklessly. On the other hand, the external constraint on credit imposed by the gold standard has gone. Central banks now virtually ignore the pace of credit expansion so long as inflation is under control. As a result, the "elasticity" of private credit creation has increased significantly.

Until the 1980s, in most economies the growth of credit was constrained in some way. After the gold standard collapsed, this discipline had been provided by tightly regulated financial markets. Most countries had some sort of credit controls that restrained the financial cycle, but at a severe cost to resource allocation. Since then governments have set their financial systems free. In the 1980s money-supply targets helped to curb credit, but these, too, were abandoned as the various measures of money sent out confusing signals.

Messrs Borio and Lowe argue that today's combination of a liberalised financial system, a money standard with no exogenous anchor such as gold, and a monetary policy focused only on short-term inflation increases the risk of longer and bigger build-ups in credit. That makes asset-price and debt bubbles more likely.

Swings in credit growth and asset prices have always played an important part in business cycles, but their role seems to have increased of late. Financial deregulation and innovation have increased the scope for more pronounced financial cycles which, in turn, can amplify the business cycle. For instance, rather than holding loans on their books, banks now bundle loans into securities and sell them on the secondary market. The resulting stream of liquidity allowed the banking system to lend more during the boom. New financial instruments and greater competition in the mortgage market have made it easier for households to borrow.

The increase in debt since financial liberalisation is not necessarily a bad thing: savings are better channelled to borrowers with profitable investment opportunities than lying idle under the mattress. However, easier access to credit can encourage overborrowing, which leaves the economy more vulnerable to a recession. Over the past decade the deepest downturns have tended to be in countries that had previously seen big increases in debt. Now it is America's turn.



Cycles in credit and asset prices usually occur in tandem, reinforcing one another. Rising asset prices boost growth and make it easier to borrow by raising the value of collateral. Faster growth in credit and output then feeds back into higher asset prices. When asset prices fall, the process goes into reverse. More households now own houses and shares, so swings in asset prices have a bigger effect on the economy.

Riding the risk cycle

In its 2001 annual report the BIS argued that the financial system tends to be too pro-cyclical because of a misperception by banks and markets about how risk moves over the cycle. Lenders tend to underestimate risk during booms, when collateral values are rising and profits are strong. They reduce their lending spreads and loan provisions, and extend too much credit. In recessions, lenders' perception of risk rises too late as borrowers default, so they tighten their lending standards and raise provisions. All this amplifies the business cycle, extending booms and increasing the depth or length of downturns.

Some economists worry that the new Basel Accord on banks' capital standards could make things worse. From 2006 banks will have to adjust their minimum capital requirements over time, in line with changes in measured risk. The danger is that banks' internal risk assessment will vary more than it should over the course of the cycle, leading to undesirable reductions in capital cushions during booms and increases during recessions. That would make the financial system even more pro-cyclical than at present.

Should central banks try to curb unsustainable credit and asset-price booms? The usual answer is that policymakers are unlikely to make better judgments about risk and sustainability than does the private

sector. But as Keynes once wrote, "A 'sound' banker, alas!, is not one who foresees danger and avoids it, but one who, when he is ruined, is ruined in a conventional way, along with his fellows, so no one can really blame him." Central bankers are less likely to run with the herd. They have longer time horizons and different incentives, as well as a better understanding of the feedback between the financial sector and the real economy, so they may respond differently to the same information.

One policy option is for capital requirements to be increased during a boom if supervisors see a potential increase in risk. Or, to cool a housing boom, regulators could restrict the maximum mortgage as a percentage of a property's value. But it would be tricky to identify exactly when this should be done. If regulators got it wrong, they might undermine the efficiency of the banking system.

The alternative is to raise interest rates to check an unsustainable rise in credit and asset prices. However, not only is it difficult to identify financial imbalances early enough to act, but central banks do not have a mandate to prick bubbles. They already do take account of rises in share or house prices to the extent that these feed into higher spending and hence future inflation, but asset-price and debt bubbles can build up with little immediate effect on inflation. Higher interest rates would be hard to explain to the public if today's inflation were well under control.

Moreover, there are doubts about the effectiveness of higher interest rates in containing share prices. Interest rates are more like a blunderbuss than a laser-guided weapon. A small rise in rates might be counterproductive if it increased confidence in the central bank's anti-inflation commitment and so boosted asset prices further. A big rate rise would probably work, but it might lead to a deep recession.

Because of these uncertainties, most central bankers believe they should not raise interest rates to stop a boom in asset prices and credit, but wait to see if the asset-price bubble bursts and then respond to the adverse consequences. That is what the Fed did last year. But prevention is surely better than cure. The BIS concludes that although caution is required in tightening monetary policy or adjusting supervisory instruments, this should not rule out the occasional use of such policies when serious financial imbalances threaten economic and financial stability.

"Identifying a bubble in the process of inflating may be among the most formidable

ble challenges confronting a central bank," said Alan Greenspan in 1999. It is impossible to determine a share's fundamental value, so, it is commonly argued, central banks should ignore asset-price booms other than where they have a direct effect on inflation.

But the emphasis on asset prices alone is wrong. It is when a boom in asset prices is combined with a big increase in debt that it becomes really dangerous, because when house prices or share prices fall, borrowers get squeezed. There is therefore a stronger case for tighter monetary policy when a surge in asset prices goes hand in hand with rapid credit growth. In their study, Messrs Borio and Lowe, looking only at information available to policymakers at the time, concluded that a simultaneous explosion in both credit and asset prices usually provided a useful warning of financial problems ahead.

The argument that central banks should act only when they are absolutely certain that they are dealing with a bubble does not stand up. Central banks have to deal with uncertainty all of the time. For

example, the uncertainties over the size of the output gap are also large. The real issue is whether central bankers are prepared to start arguing the case for raising interest rates in response to serious financial imbalances, and whether they are prepared to live with unpopularity if they burst a bubble in equities or house prices. Mr Greenspan would not be so revered today if he had intentionally pricked America's stockmarket bubble.

With hindsight, the Fed should have raised interest rates much sooner in the late 1990s. Its failure to do so is an understandable mistake, because with inflation so low it would have come under political attack. Less forgivable was Mr Greenspan's irrationally exuberant endorsement of the "new economy", which contributed to the euphoria. Productivity growth has increased, but an official at another central bank argues that it would have been wiser if he had remained more agnostic, rather than acting like a fireman-turned-arsonist.

Views about how the economy works and what role monetary policy should play have changed many times in recent

decades. From the 1950s to the 1970s the main objective of monetary policy was full employment. Once inflation took off, governments abandoned full employment to make the control of inflation their number one priority. Persuading the public that credit and asset-price bubbles are just as bad for them as inflation is surely no harder than making the switch from fighting unemployment to fighting inflation.

During the past century, every monetary rule has broken down in the face of changing economic circumstances: the gold standard, the Bretton Woods system of fixed exchange rates, and monetary targeting. Now it seems that strict inflation targeting is not the promised panacea either. Central bankers' fixation on short-term price stability can blind them to other important signs of financial imbalance. In turn, those imbalances can cause deeper recessions and even a future risk of deflation. Without some redesign of monetary policy to take more account of swings in credit and asset prices, economic booms and busts could well become more disruptive in future. ■

United we fall

WHEN America sneezes, the rest of the world catches cold, and last year the effect of America's downturn on the rest of world seemed more brutal than usual. As America went into recession, the euro area's economies ground to a halt, Japan's slump deepened, and emerging economies from Mexico and Argentina to Singapore and Taiwan suffered deep recessions. Does global economic integration mean that business cycles now move more closely in step?

Economies have often been hit simultaneously by common global shocks, such as the jump in oil prices in the 1970s. However, during most of the 1990s business cycles were unusually desynchronised because of shocks that affected only particular countries. When the American economy stumbled in 1990, German unification kept continental Europe aloft until 1993, and Japan, buoyed by rising land prices, continued to boom until 1992.

In contrast, last year's global downturn was unusually synchronised. According to J.P. Morgan, an American bank, the disper-

sion of growth rates across 41 economies fell to its lowest level in at least 30 years (see chart 11). Some of this was due to common factors, such as the bursting of the IT bubble and higher oil prices. But it seems that different economies' business cycles are also becoming more closely correlated over time, possibly because of greater

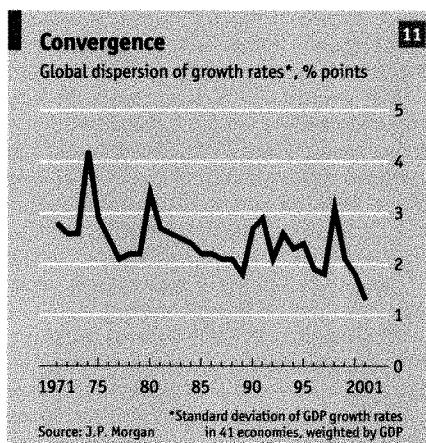
Increasing globalisation could lead to bigger economic booms and busts

economic integration.

It used to be argued that increasing trade would stabilise GDP. In a recession, exports could offset the slump in domestic demand; in a boom, spare overseas capacity would help to hold down inflation. But increased trade also causes economies to move more closely in step. Last year an investment slump in America spread quickly to Asia as American firms imported less IT equipment. In turn, Asian economies bought less from the United States and elsewhere, which depressed growth further. Greater synchronisation is likely to exacerbate the business cycle.

World trade now accounts for 25% of GDP, double its share in 1970. However, trade figures understate the degree of international interdependence. Foreign direct investment, cross-border mergers and financial markets have an even bigger effect.

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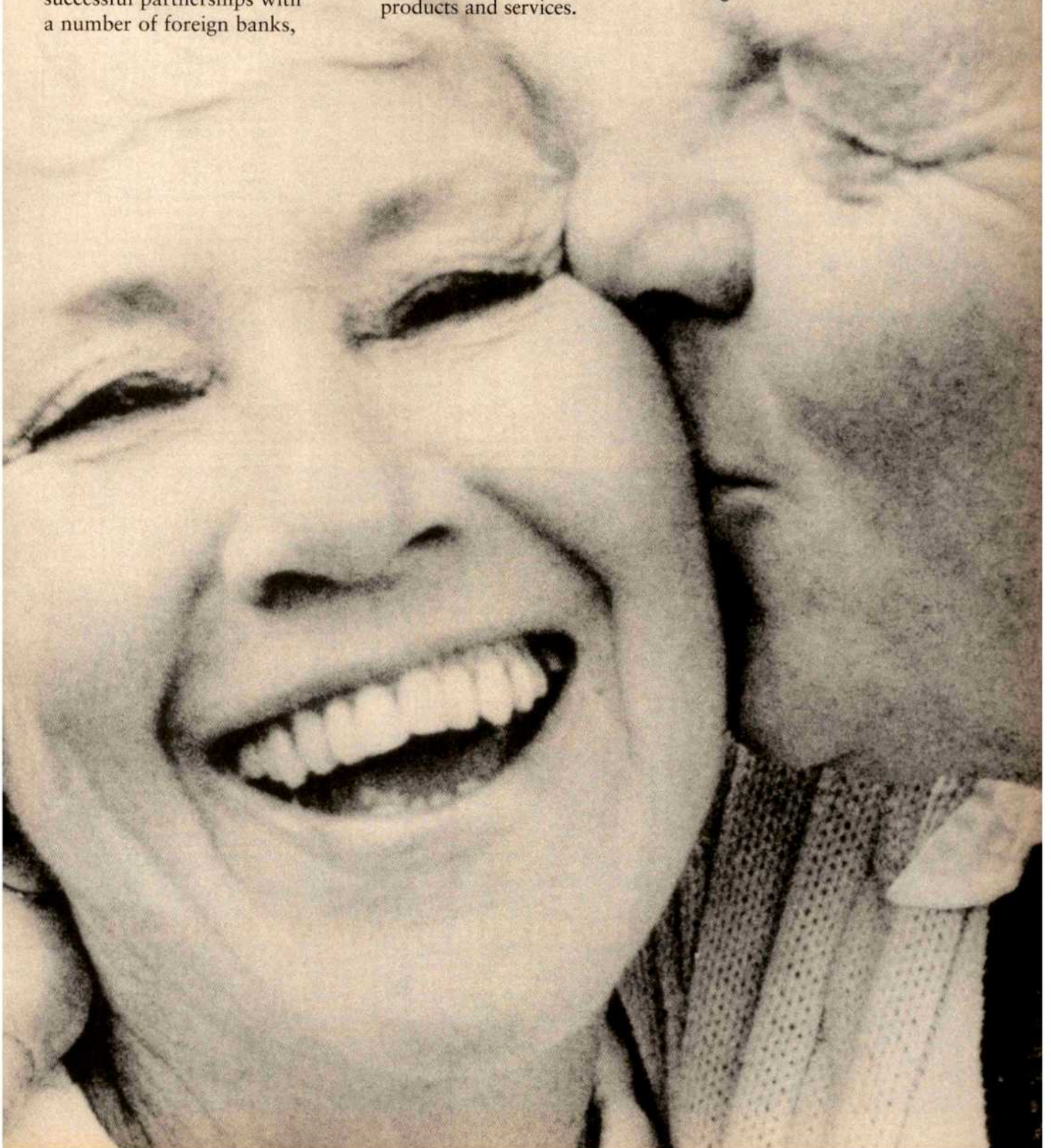
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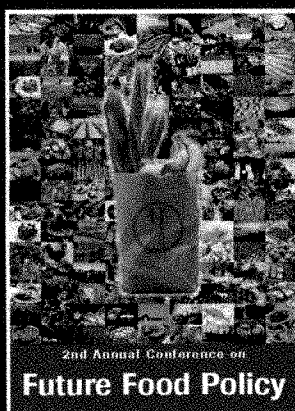
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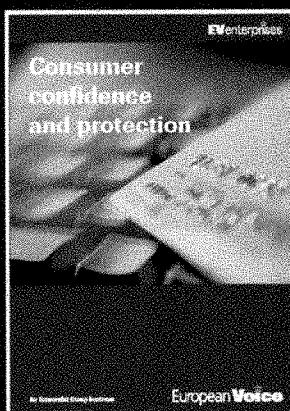
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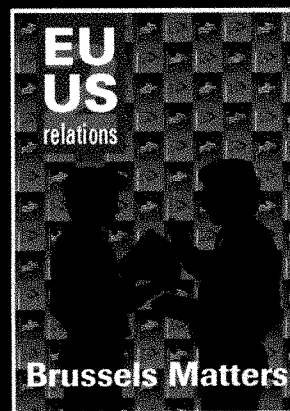
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► use of comparative advantages, such as cheap or highly skilled labour. Foreign direct investment has increased the importance of international trade within firms. One-third of both America's and Japan's total trade takes place within multinationals and their affiliates. The share of intra-firm trade is especially high in the IT sector, which is why the IT investment bust spread so rapidly around the world. The OECD concludes that thanks to the internationalisation of production, a demand shock in one country will have wider international effects than in the past.

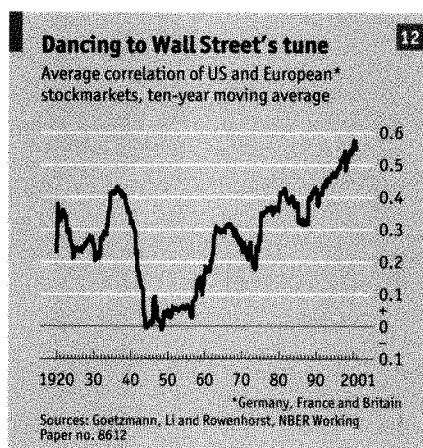
For many multinational firms, foreign direct investment has also become a substitute for trade. For example, a German car maker will produce locally in America rather than exporting there. European firms' dollar sales from their American subsidiaries are now four times bigger than their exports to America. The slump in America last year squeezed such parent firms' profits, prompting some cutbacks in Europe. American multinationals also responded to the slump at home by cutting back at their European subsidiaries.

It's the same the whole world over

Financial markets are another important channel for transmitting shocks across borders. Stockmarkets in Europe have fallen by just as much as Wall Street over the past two years. William Goetzmann, an economist at Yale School of Management, calculates that in recent years the correlation between the markets of America, Britain, France and Germany has been closer than at any time in the past century (see chart 12). The cost of capital for European firms may therefore be more sensitive to ups and downs in America than in the past. A collapse of share prices on Wall Street will also have a bigger effect on wealth and spending all around the globe.

There are many reasons why share prices are dancing to the same beat. Cross-border trading in shares has increased hugely over the past decade, creating a global equity market. In most rich countries, household are increasingly investing in foreign equities. Many big firms are also listed on more than one stockmarket. And thanks to cross-border mergers and foreign direct investment, a growing slice of firms' profits comes from abroad.

Is the recent close-coupling of national stockmarkets a temporary phenomenon, caused by the IT bubble and the consequent global slowdown, or does it reflect the growing international integration of firms? Robin Brooks, an economist at the



IMF, and Marco Del Negro, at the Federal Reserve Bank of Atlanta, tried to discover whether the increased correlation of stockmarkets can be explained by firms becoming more global, as measured by the percentage of their sales and profits that are generated abroad. They analysed company accounts and share prices for 10,000 firms in 42 markets over the period 1985-2002, and found that such global factors had indeed become more important in explaining variations in companies' profits in the late 1990s. Global factors were especially important in explaining the relative share prices of firms that derive a high proportion of their profits from overseas. This suggests that the rise in stockmarket correlations in the late 1990s may indeed reflect global integration. If so, it is likely to increase further over time.

Another way in which recession can spread from country to country is through business confidence. The IMF finds that there has been a substantial increase in the correlation between business confidence in America and the euro area in recent years. This probably reflects the stronger links between firms in America and the euro area through mergers, as well as the

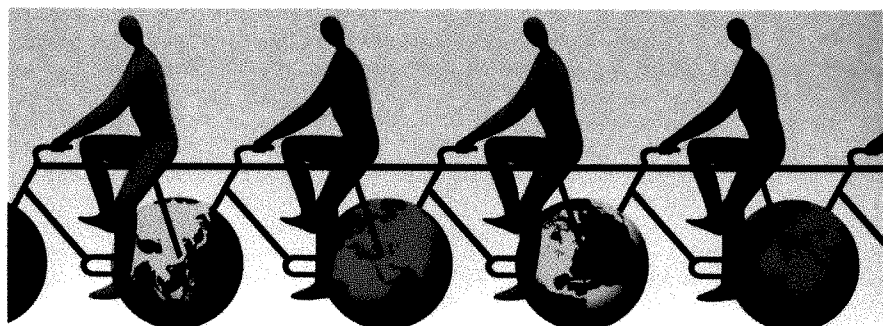
effect of global share prices on business confidence. Either way, the mood of businessmen can be a lethal form of contagion.

As economic and financial interdependence continue to increase, developments in one economic area will affect other economies more than in the past. As a result, global business cycles are likely to become self-reinforcing, which could make booms and recessions in developed economies more severe.

Policymakers clearly need to take more account of what is happening in other countries. Traditional economic models that look only at trade will understate the effect of a shock in America on other economies. Foreign investment, share prices and confidence are likely to be far more important. The ECB was caught out last year when it underestimated the impact of America's downturn on the euro area. Even though Europe did not suffer from the sort of imbalances seen across the Atlantic, its economies stumbled as falling equity markets hurt business confidence.

Does growing economic interdependence increase the case for international policy co-ordination? In the past, attempts at this by the G7 group of rich countries have had unhappy consequences. At the Bonn summit in 1978, Germany agreed to reflate and act as the world's locomotive. But oil prices then surged, triggering a burst of inflation. In the late 1980s, at the Louvre meeting, Japan agreed, under pressure, to ease its monetary policy in return for America cutting its budget deficit. Many now regard this as a prime cause of Japan's financial bubble.

The regular exchange of information and frank discussion about policy in each other's economies is useful. But, wisely, the G7 have avoided formal agreements to co-ordinate policy in recent years. The best global economic policy is the sum of the best national policies that take account of developments elsewhere. ■



After the bubbles

Brace yourself for a bumpier time ahead

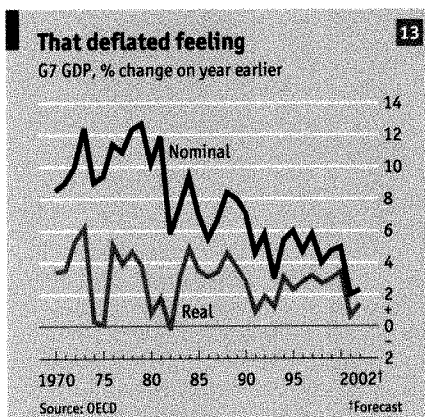
DESPITE the slump in share prices, most economists reckon that America's economy will continue to recover this year. They believe that the post-bubble recession was mild thanks to the Fed's superb monetary policy and the American economy's amazing flexibility. In reality, though, America's first recession of the 21st century may not be over.

The optimists base their forecasts on their belief that America's economy is "fundamentally sound"—or as sound as an economy can be with inadequate saving, far too much debt and a massive current-account deficit. America not only had a stockmarket bubble in the late 1990s, it experienced a wider economic bubble that distorted decision-making across its whole economy. This created excesses that need to be purged before the economy can return to vigorous and sustainable growth.

Firms have made great strides to cut costs and capacity, yet corporate debts still look uncomfortably large, so further pruning is likely. Troublingly, consumers have continued to borrow as if little has changed. By slashing interest rates, the Fed has encouraged a house-price boom that has partially offset equity losses and allowed households to take out bigger mortgages to prop up their spending. But for how long? House prices are high in relation to income, so the room for further gains is limited. Households' debt-service payments are also close to a record high, even though interest rates are low.

Households cannot keep borrowing at their current pace. At some stage they will need to start saving more and spending less. If this happens abruptly, it will trigger another, deeper recession. If instead the adjustment is made gradually, America could face several years of sluggish growth of less than 2%. That would be well below the economy's trend growth rate, so unemployment would rise. In this sense, America's "recession" is far from over.

Could America follow Japan into a decade of stagnation? The popular perception is that America's economy has held up much better than Japan's did after its own stockmarket bubble burst in December 1989. Yet America's economy now looks awfully like Japan's in the early



1990s, when Japanese investment fell but consumer spending and productivity growth remained robust for a couple of years. Deflation did not appear until 1995. America may yet face further troubles.

There are, of course, big differences between the two economies. Market forces work better in America's more flexible and competitive economy, so excess capacity is likely to be scrapped and capital reallocated more speedily than in Japan. America's economy is also much less dependent on banks than Japan's, relying more on capital markets as a source of finance for firms. Capital markets, unlike banks, re-price assets immediately instead of deferring the pain. Japan's sick banks have also been unable to make new loans, which has delayed recovery. American banks are in much better shape.

A third point in America's favour is that its political system is less rigid than Japan's. If politicians fail to deliver economic recovery, in due course they will be replaced. In Japan the LDP is still in power, despite a decade of near-stagnation. The result is policy paralysis.

Nevertheless, American policymakers cannot afford to be complacent. The list of differences between Japan and America has got shorter over the past year. America, it used to be argued, had better corporate governance and more accurate financial accounts than Japan. Enron and WorldCom have exposed that myth. America, it was said, had only a stockmarket bubble, whereas Japan also had a

property bubble. The rapid growth in house prices and mortgages in America over the past couple of years is starting to look suspiciously bubble-like.

Last, but not least, America supposedly had plenty of room to cut interest rates, so it could avoid deflation. But by now the Fed has shot most of its ammunition: with interest rates and inflation already so low, there is little room for further easing if the economy stumbles. That raises the spectre of falling prices, which would be devastating in an economy so awash with debt.

Some Europeans may be tempted to gloat over America's misfortunes. But if America sinks back into recession, it will take much of the rest of the world with it. As America's current-account deficit becomes harder to finance, a sharp fall in the dollar will export deflationary pressures to other countries. Worse, policymakers in Japan and the euro area currently seem unwilling or unable to offset such a shock.

Measured by real GDP, last year's global recession was relatively mild, but nominal GDP growth in the G7 economies fell to its slowest rate for decades (see chart 13). In this year's "recovery", nominal GDP growth is running at just over 2%, less than the typical rate seen during other recessions since the second world war. In this sort of environment, it becomes much harder for firms to increase their profits and work off their debts. Most companies, investors, households and policymakers have never experienced anything like it during their lifetime.

A false sense of security

Current wobbles aside, most analysts still assume that the greater economic stability of recent decades will continue. They hope that it will allow firms to go even further in eliminating the inventory cycle, and that sound monetary policies will continue to prevent the high inflation rates that caused economic instability in the 1970s. That would have important implications. A more stable economy is a less risky economy, which would justify a lower equity-risk premium. Historical price-earnings ratios would then be irrelevant, so share prices might now be undervalued. And if incomes and profits fluctuate



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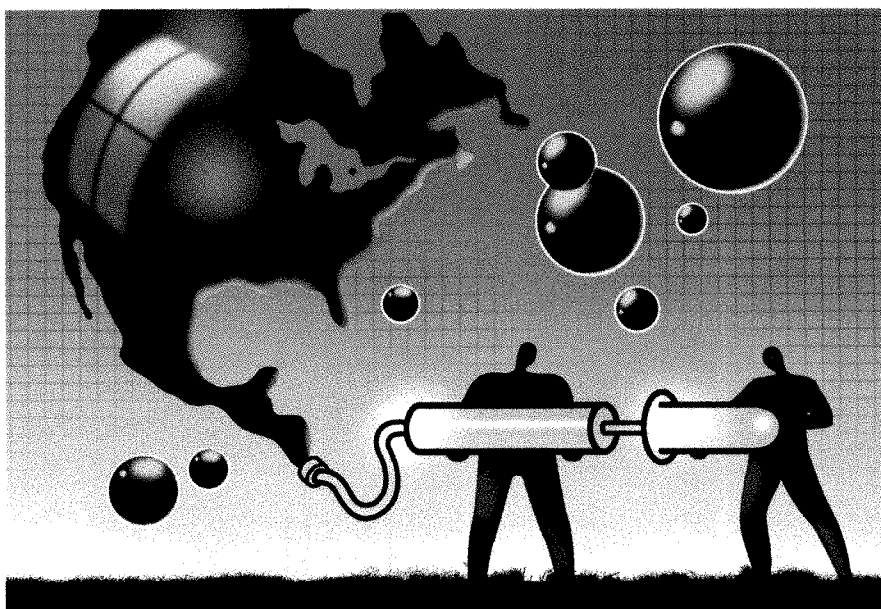
ate less over the cycle, then households' and firms' current large debts might prove perfectly manageable.

However, this survey has identified several factors that might make the economic cycle more rather than less volatile over the coming years, thus prompting investors to demand a higher risk premium. One consideration is that America's enhanced economic stability in the 1990s was in large part due to luck, such as the unusually desynchronised nature of business cycles in the main economies. This helped to curb the usual inflationary pressures during America's boom, allowing it to continue for longer. In future, as economies become more internationally integrated, economic cycles are likely to move much more closely in step. If everybody sinks together, recessions could be deeper.

A second cause for concern is that fiscal policy may be less able to cushion downturns than in the past. There is some tentative evidence that fiscal policy is becoming less potent as economies become more open. More worrying, in some circumstances monetary policy may also prove to be a blunter weapon. If central banks try to hold inflation too low over the cycle, they will leave themselves too little room to ease policy in a deep recession, because it will be harder to deliver negative real interest rates. In the next cycle inflation and interest rates could peak at a lower level than in the last one, and as inflation gets closer to zero economies become more unstable, as Japan has discovered. This is not to argue for a return to double-digit inflation, but to suggest that central banks should aim to keep inflation above 2%.

Even then, low inflation can amplify the business cycle in another way. In the 1970s and 1980s high rates of inflation allowed inflated asset prices to adjust back to their fair values without the need for a big drop in nominal prices. For instance, British property prices in the four years to 1993 fell by 25% in real terms, but by only 8% in nominal terms. If today's boom in house prices around the globe does turn out to be a bubble, then with such low inflation house prices would need to fall more sharply in absolute terms to bring the market back into balance. That would be painful for those with big mortgages.

In a world of low inflation, excessive swings in asset values are therefore even more dangerous. Yet this survey has argued that financial liberalisation, combined with central banks' single-minded emphasis on inflation, has increased the risk of asset-price and credit bubbles. Ja-



pan in the 1980s and America in the 1990s could be just the first of many.

Moreover, equity and property prices are not only likely to be more volatile, they will also have a bigger effect on consumer spending than they used to. As people live longer after retirement and the average age of populations increases, more people will be dependent on the value of their assets, in the shape of both property and equities, rather than income from employment.

After a period of relative calm, the business cycle is likely to become bumpier again. What does this mean for policymakers? Until recently, central banks believed that so long as inflation was kept firmly under control, booms and busts could be avoided. Yet in reality low inflation does not guarantee stable growth. If central banks are to prevent bigger booms and busts in future, they need to take a broader view and sometimes act to curb excessive growth in debt and asset prices.

A second lesson is that governments

need to do more to enable economies to cope with volatility. Flexible markets, stronger financial institutions and better corporate governance can help to minimise the cost of recessions. If Japan and the euro area were to press ahead with reforms, it might also help to boost their domestic growth, reduce their dependence on America, and so partly offset the growing synchronisation of economies.

The third and most important point to remember is that the business cycle will never be eliminated; it is part of human nature. Indeed, once people think that the cycle has become a thing of the past, they act in ways that sow the seeds of the next recession. If central banks succeed in postponing a recession, they will simply encourage more reckless behaviour, making the next downturn worse. A recession once in a while may actually be a good thing, as long as it is not too deep. It reminds companies, households and investors of that other R-word: risk. ■

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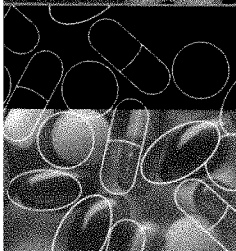
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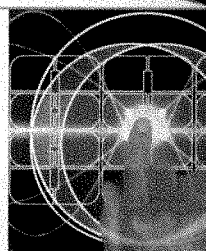
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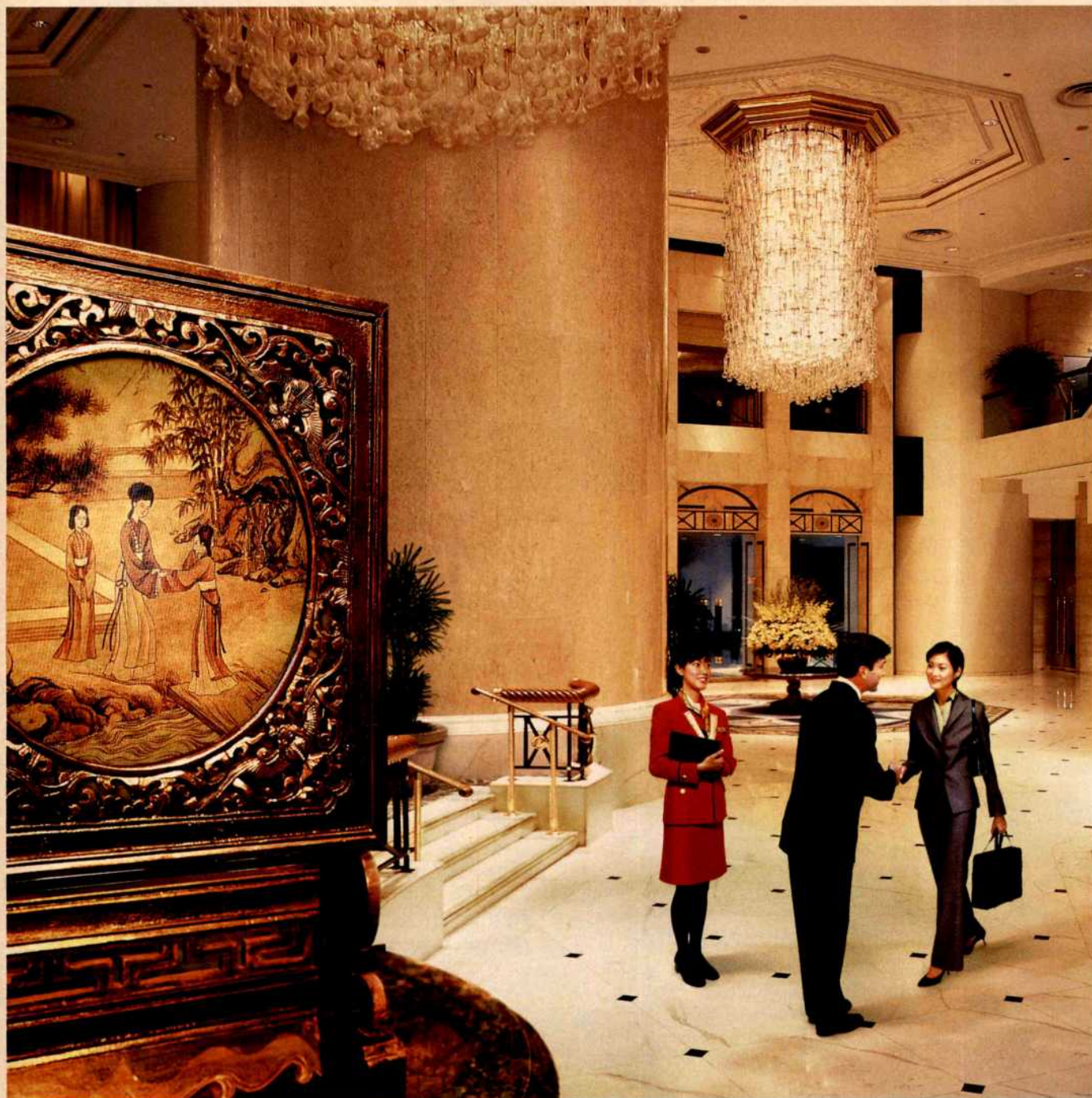
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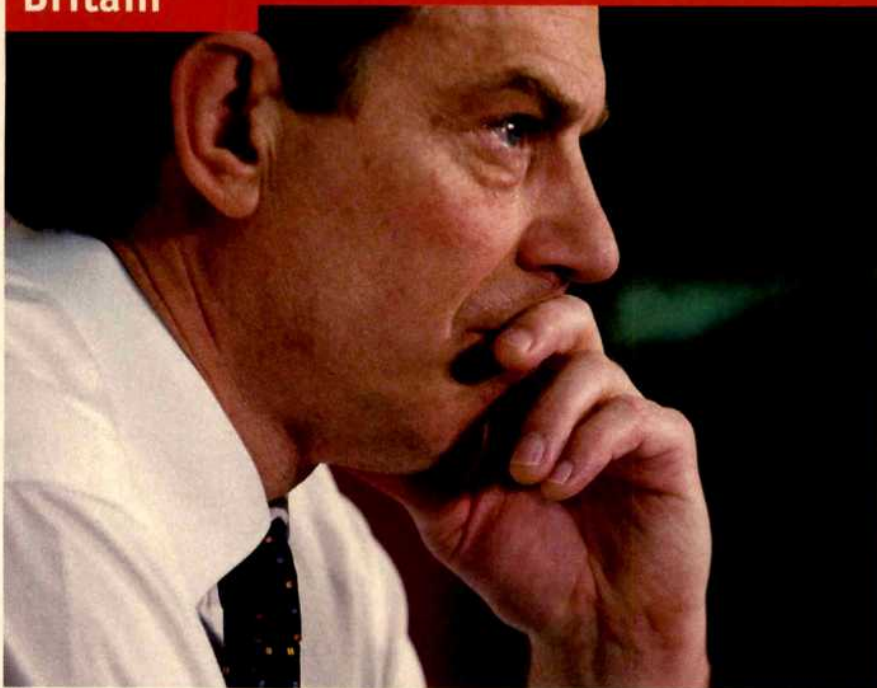


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Blair's government

Should try harder

A report card on the government's performance on improving public services

HAS the government been cheating pupils taking A-level exams by encouraging examiners to downgrade marks? Has the education secretary, Estelle Morris, been interfering with the inquiry into the exam fiasco, as the head of the government's exams watchdog says she has? As *The Economist* went to press, these questions remained unanswered. But the fact that they were being asked made this week a dreadful lead-in to next week's Labour Party conference, at which the government's domestic record will come under unaccustomed scrutiny.

The party knows that Iraq is unlikely to have much bearing on the the next elec-

tion. It is domestic affairs—especially the promised improvements in public services—that will matter most. And on that front, things have not been going so well.

The government has been pouring money at an accelerating rate into the public services. Spending by government departments is rising in real terms by 6% this financial year and will be 22% higher than in 1998-99. Conscious of Labour's past reputation for profligacy, Tony Blair has always sought to reassure taxpayers that this is a reform-and-spend rather than a tax-and-spend government. The avalanche of extra cash has been accompanied by a bristling array of purportedly tough tar-

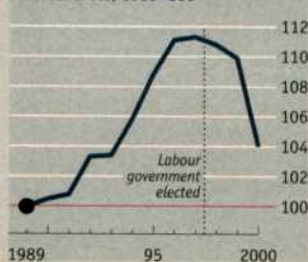
gets and by commitments to open the public services to greater competitive pressure.

But for all this, not much has improved. Spending on the National Health Service in this financial year is £20 billion (\$30 billion) higher than in 1998, but much of the extra money is going into higher pay. More staff, especially nurses, have been recruited, but overall productivity has fallen (see first chart). Very long waiting times (more than a year) have fallen, but the waiting list for treatment in hospitals is still over 1m patients—about the same as in 1996. "The next step, of getting waiting times below a year, is far more difficult," says Anthony Harrison of the King's Fund, a health-policy think-tank. Performance ratings show that 47 of the trusts that run hospitals in England improved between 2000 and 2001 but 36 deteriorated. Waiting times in accident and emergency departments have got worse since Labour came to power.

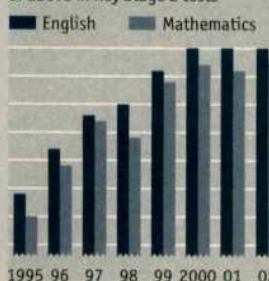
Labour has a better story to tell on education, especially in primary schools (see second chart). But the improvement began

Things can only get better...still!

NHS productivity, measured by cost-weighted activity per unit of real resources, 1989-2000



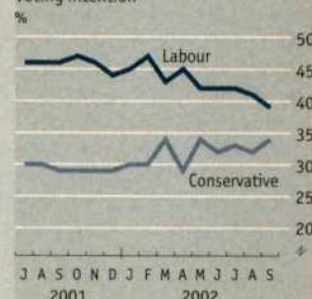
% of 11-year-olds achieving Level 4 or above in Key Stage 2 tests



Do you agree or disagree: In the long term, this government's policies will improve the state of Britain's public services*



Voting intention



Sources: Julian Le Grand; Department for Education and Skills; MORI Social Research Institute Delivery Index; ICM

*Balance of those who agree minus those who disagree

before Labour took office in 1997 and stalled after 2000. As a result, the government has failed to meet its original targets for 2002—for expected standards in maths and English to be reached by 75% and 80% of 11-year-olds. And progress in the performance of 14-year-olds has been more modest.

As education secretary, David Blunkett pledged that he would resign if the government failed to meet its targets for 11-year-olds. In his new role as home secretary, he is finding the going no easier on another public service that voters care intensely about: maintaining law and order. Total recorded crime increased at an underlying rate of 2% in 2001-02, with some violent crimes increasing faster: robbery, for instance, rose by 27%.

In all these services, Labour's preferred method of promoting improvement—the use of performance targets—increasingly prompts derision rather than respect. The government's waiting-list target for the NHS in its first term of office led some hospital managers to fiddle their figures. There is widespread mistrust of government claims of success in the war against crime. Labour's use of targets—without independent scrutiny of its performance—commands less and less credibility. The use of targetry has another disadvantage: it alienates staff. More than three-quarters of people who leave the public sector blame the regime of central control and the paperwork that it engenders, according to a recent report from the Audit Commission.

This is why Mr Blair's commitment to give private providers a bigger role in the public services was potentially so important. Unlike the managerial techniques of targets and performance management, this has the potential to ginger up the public services through real competition. But despite the prime minister's rhetoric, the private sector has been largely confined to financing and then maintaining capital projects like new hospitals. The spread of private provision into core public services like medical care or schools has been glacial. Only a handful of schools are being run as public-private partnerships.

Trade union opposition helps explain this failure. Three-fifths of public-sector employees belong to unions, compared with a fifth in the private sector. The unions fear that greater private provision will erode their power. "Labour isn't willing to take the unions on even though it clearly sees them as a massive impediment to improvement," says Tony Travers of the London School of Economics.

Spending without reform clearly suits the unions nicely. If higher expenditure on public services comes to be seen as payday for public-sector workers, Labour will lose the reputation for prudent economic management which it struggled so hard to win in its early, parsimonious, years. ■

Britain, America and Iraq

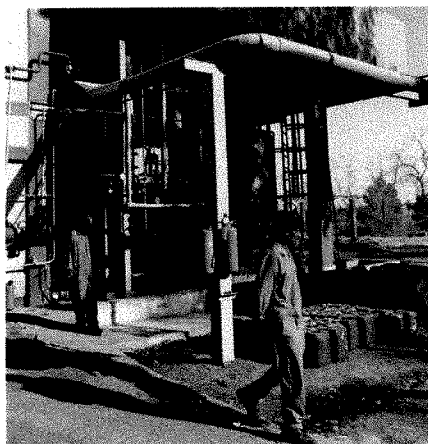
Tony's dossier

What Saddam's got and what he's not

PRESENTING his "case against Iraq" in the form of a 50-page dossier, outlining the Baghdad regime's unconventional military ambitions, its lies to the UN and its human-rights abuses, Tony Blair got a calmer-than-expected reception in the House of Commons. Only 53 members of his own party voted against the government. It was one of the biggest backbench rebellions since Labour came to power, but Tories and Liberal Democrats abstained, and no government member wobbled.

In a well-crafted appeal to common sense which takes care not to seem hyperbolic, the dossier presents evidence that Iraq possesses and is continuing to produce both chemical and biological weapons; and that it is trying hard to acquire nuclear weapons. It says Iraq has tried to buy uranium for a nuclear weapon from an unspecified African country. In a very British attempt to be fair, the document concedes that as long as existing UN sanctions remain in place, and as long as Iraq does not manage to obtain nuclear material from some covert source, then it will not be able to produce nuclear weapons. But if it does succeed in getting fissile substances on the black market, then it could go nuclear in a year or two.

The document also made fresh allegations about the ballistic missiles which Iraq either has or wants—in defiance of UN-imposed resolutions that restrict the range of Iraqi rockets to 150 kms (94 miles). It alleges that Baghdad has illegally held on to up to 20 missiles with a range of 650 kms; has built an engine-testing facility as a step towards developing a 1,000-km rocket; and is trying to extend the reach of



Last one out turn off the gas

The language of war

You say potato

What Britain means by regime change

IS REGIME change in Iraq the British government's policy, as it seems to be the American government's? That central question was put to the foreign secretary, Jack Straw, in the course of an interview on the BBC's *Today* programme. His answer seems to be that it is, with a crucial difference: while in America, "change" means "removal", in Britain it means "improvement". Here's what he said:

If there is to be disarmament by the Iraqi regime under Saddam Hussein, then the nature of that regime will have to and will have changed quite profoundly, because its weapons of mass destruction which are the basis of the evil power which it has will have been removed.

So that's all clear, then.

its short-range missiles. Non-conventional weapons, the report says, play a key part in Iraq's defence doctrine, which provides for strikes with poison gas or germs within 45 minutes of an order being issued.

"I defy anyone to say that this cruel and sadistic dictator should be allowed any possibility of getting his hands on chemical, biological or nuclear weapons," the prime minister declared, after drawing Parliament's attention to a catalogue of Iraqi war crimes and human-rights abuses, including grisly photographs of children who died in the chemical attack on the town of Halabja in spring 1988.

Heart-rending as these pictures are, they also have some drawbacks as a presentational device, as Mr Blair discovered during the debate. Mohammad Sarwar, a Labour MP from Glasgow, challenged the prime minister to admit that Britain and America had actively supported the Iraqi regime during its worst days as a user of chemical weapons.

Wrong, Mr Blair insisted; there had been "presidential statements" from the UN Security Council rebuking Iraq. (That is true up to a point: the reason why the UN issued statements—as opposed to resolutions—is that the latter would have been vetoed by America. And both America and Britain did go on issuing trade credits to Iraq as its chemicals rained down.)

In any case, proving Saddam Hussein's wickedness was always going to be the easy part of Mr Blair's propaganda strategy. Without a miraculous change of heart in Baghdad, he will now face the harder task of arguing that a \$200 billion war is the only way to disarm Iraq, and that Britain should fight in it alongside America. ■

Celebrity economics

Land of hoped-for glory

The media's new high-volume, low-cost product: talentless celebrities

FAME is a funny business, and a booming one too. Last weekend Britain's most down-market and celebrity-obsessed daily newspaper, the *Daily Star*, launched a Sunday edition. On September 25th, Emap, a big magazine publisher, launched a sister magazine for its existing and highly successful weekly *Heat*, which sells around 480,000, roughly the same as its main competitors, *Hello* and *OK!*. The new rag, *Closer*, is aimed at an older audience, includes a bit more real journalism, and plans to sell around 300,000.

There are two trends here. One is that public appetite for celebrity news of all kinds is unsated. That reflects social changes such as television's dominance of leisure time, and, maybe, the breakdown of real communities and the consequent substitution of gossip about known people with gossip about unknown ones. The other shift is that manufacturers of fame are trying to make sure that they, rather than the celebrities, get the money.

That means using disposable celebrities rather than real stars. Truly talented people—actors, writers and so on—are in a sellers' market. As Hollywood studios have found, stars are demanding, and getting, an ever-bigger share of the cake.

The solution is to shift the balance between fame and talent. In the past, fame was won by achievement. Now, media companies have realised that celebrities are their main input, so they need more of them. As a result, exhibitionism alone can lead to fame, through an appearance on a television game show or reality TV. Being the relative of someone famous helps too. In a recent, particularly grotesque, British reality TV survival show, one of the leading "celebrity" participants, Christine Hamilton, was famous only for being the wife of a disgraced politician. The only talent she has displayed is for self-publicity.

Talentless celebrities are easier to manage, cheaper to produce, and much more lucrative than real stars. "Most of these people are in effect working free for the media moguls," says Matthew Freud, one of Britain's top publicists. Reality TV draws millions of viewers. In print media, a famous face on the cover pushes up sales; so does a scandalous or salacious story. But the micro-celebrities themselves have a weak bargaining position. Most participants in "Big Brother", Britain's first reality TV show, made less than £30,000 (\$45,000) for their public humiliation, Mr



Fame can seriously damage your looks

Freud reckons. The current crop of reality shows crowding the autumn schedules should drive rewards down even further.

Competition from the talentless makes life tough for those a few rungs up the ladder. They can no longer rake in big fees for, say, exclusive pictures of their bathrooms. Mrs Hamilton (see above) and her husband Neil are reportedly (according to a celebrity magazine) planning a Christmas pantomime appearance. Fine for them, but tough on whichever minor soap opera actor they have displaced.

Prince Charles

It really is appalling

Writing letters is a harmless pastime. Until they are leaked

UNDEREMPLOYED celebrity seeks job as lobbyist. For more information contact charles.windsor@stjamespalace.co.uk. An advertisement along those lines would be a fitting end to this week's furore about Prince Charles's leaked letters to the government.

On the face of it, the concerns the heir to the throne raises, apparently every couple of weeks or so, about the consequences of litigation mania and bureaucracy are quite reasonable. It is absurd for a local council to cut down perfectly good horse chestnut trees for fear that pedestrians will sue if they are hit by conkers. Overly pedantic standards in care homes—where hygiene regulations, for example, prevent volunteers bringing in food for old people—are so excessive that even the government has now agreed to apply them more laxly. It is hard to imagine that the armed forces will function better if relatives of dead servicemen can sue the commanding officer.

If Britain had a proper opposition

Instant celebrity is a fleeting asset because if there is no real achievement to interest the public in—no stage or screen triumphs, no interesting books, no heroic exploits—people quickly become bored. To turn celebrity into cash you have to be wily, or well-advised. Geri Halliwell, for example, a former Spice Girl, found that her solo album flopped. Her clever managers rushed out an exercise video, which sold very well. The public, it turned out, was interested in Ms Halliwell, but preferred looking at her to hearing her sing.

Some punters, of course, still drool over simple snaps of the home life of minor royalty, but the growth in the celebrity industry is elsewhere. *Heat*'s success reflects an innovative, more waspish approach, aimed at young women who might otherwise buy mainstream magazines such as *Elle*. *Closer* will mix celebrity news with real life stories (the lead story in the first issue is about an anorexic five-year-old).

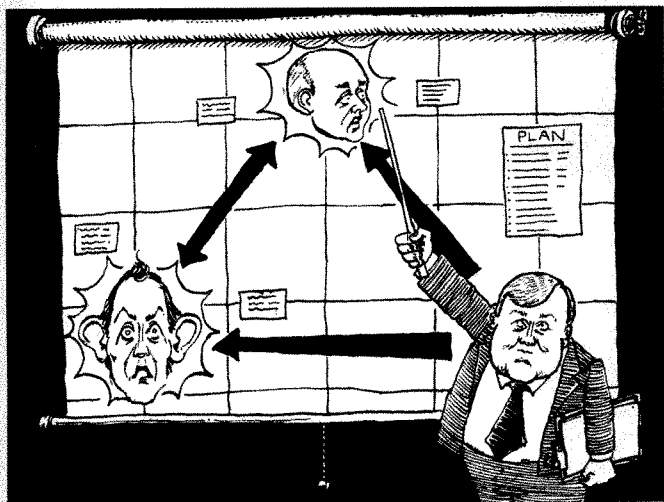
So the new structure of the business is becoming clear. There is the mass-market segment: bland, commoditised, low-margin, fast turnover, and unsavourily exploitative if you look too closely. Success is about commercial muscle coupled with shamelessness. In the middle market, doing well requires a bigger dose of brains and talent. And at the top end, real stars are reaping the rewards as never before. Nice work if you can get it: most can't. ■

party, or a less slippery government, these questions could be aired elsewhere. Although it may be irritating for ministers to receive regular letters from the heir to the throne, it is hard to see what damage they do. If they highlight a real problem, ministers may learn something. If not, they can simply ignore them. Nobody is likely to be offended: even now, there is no strong lobby in Britain for greater bureaucracy and more litigation.

The problem comes on other questions where the prince's views are ill-informed, sentimental or downright daft. According to one leak, he complained earlier this year that the government treated farmers worse than "blacks and gays". Although friends say he in fact mentioned only blacks in the letter, it still shows a remarkable inattention to the facts. Farmers are rarely kicked to death by skinheads. Blacks do not receive billions of pounds of public subsidy. A future king should know his subject(s) better.

Bagehot Kennedy triangulates

The Lib Dems have come up with an electoral strategy that could work



IT HAS been rather a good week for Charles Kennedy. Although the recall of Parliament for a special one-day debate on Iraq interrupted the Liberal Democrats' annual conference (thankfully deflecting attention from a leisurely afternoon spent discussing the merits of allowing 16-year-olds to buy hard-core porn), the clouds of war have brought with them a silver lining for Mr Kennedy.

With Iain Duncan Smith, the Tory leader, committed to playing the role of little echo to the prime minister, Mr Kennedy has been the only party leader able to give voice to the anxiety and scepticism that opinion polls suggest is felt by much of the country. "Am I alone," he asked, "in feeling increasingly concerned about this concept called regime change? I think not. Am I alone in worrying about the undermining of the moral, legal and practical authority of the United Nations? Again, I think not." Mr Kennedy, whose unassuming good humour normally robs him of the gravitas to which senior politicians aspire, managed to sound serious and principled, while still leaving himself room to support future military action if sanctioned by the UN.

If that were all, Mr Kennedy could be excused for feeling quite pleased with his week's work. But he has other reasons as well. For the first time since becoming leader of the Liberal Democrats, three years ago, Mr Kennedy appears to know where he and his party should be going. This, in part, is due to his own stepped-up efforts—the "inaction man" barb had just enough truth in it to have stung—and partly as a consequence of the way in which the political landscape is beginning to shift.

Although Mr Kennedy wisely rescued his party from the blind alley of pacts with Tony Blair in which his predecessor, Paddy Ashdown, invested so much time and hope, he had put little in its place. The strategic dilemma for the Lib Dems seemed so acute that Mr Kennedy was inclined to the view that the best strategy might be to have no strategy. In recent years, the Lib Dems have prospered modestly by attacking New Labour and Blairism from the left, in particular, making the case for higher taxes to revive under-funded public services and, all too often, supporting producer lobbies, such as doctors and teachers, in their opposition to even relatively feeble government-sponsored reforms. For a party whose sentiments are firmly to the left of centre on most things and many of whose activists are involved

in local government, it was easy and unchallenging.

There was even a degree of electoral logic in it. Although nearly all of the party's top 50 "target" seats are held by the Conservatives (Oliver Letwin and David Davis are both in some peril), many of those would fall to the Lib Dems if disillusioned Labour supporters in such constituencies could be persuaded to switch their vote.

But for all that, the shrewder Lib Dem tacticians (such as David Laws, a successful young banker who inherited Mr Ashdown's seat in Somerset, and Mark Oaten, the party chairman, who converted an 8,000 Tory majority in Winchester ten years ago into a 10,000 Lib Dem majority in 2001) knew that it would be impossible to take over from the Tories as the main party of opposition without a stronger, direct appeal to Conservative voters. Mr Kennedy too became convinced that heading to the left of Labour was "the biggest cul-de-sac in British politics".

What made it easier for Mr Kennedy to give his party a shove in the right direction was Gordon Brown's opening of the public spending flood-gates. Suddenly, the notion of bidding to outspend Labour was no longer tenable. While there might be some mileage in contrasting Lib Dem frankness about the need for higher taxes with Labour's obfuscation during the election campaign, it was limited and temporary. The one thing that everyone in British politics was able to agree on was that the issue now was delivery not money. For both the Lib Dems and the Tories everything would now depend on the expectations that the government had aroused not being met and whether they could persuade disappointed voters that they had a better way.

Mr Kennedy understood that he now had the chance to come up with a Liberal Democrat "third way" that would allow an almost perfectly symmetrical "triangulation" on both Labour and the Tories. The government, for all its talk of extra spending being "conditional on reform", had failed to escape from a model of public-service provision based on highly centralised control of both funding and standards; and whatever the Conservatives eventually came up with would be vulnerable to the charge that behind their new enthusiasm for "localism" was a hidden agenda of privatisation and tax cuts.

Something to say, at last

This week, after many months of work behind the scenes by the grandly-named Public Services Policy Commission and a certain amount of arm-twisting, Mr Kennedy succeeded in defeating a modest but noisy grassroots revolt and getting the party conference to adopt a set of proposals that set out a reasonably coherent Liberal Democrat alternative. Its most interesting elements are: a high degree of local political accountability for devolved health and education services, under-pinned by a good deal of funding coming from locally-raised income tax; an end to centralised wage negotiations and an acceptance that local labour market conditions will influence pay; and a commitment to increase consumer choice by encouraging a wider range of service providers, including new mutual-type "public benefit organisations", which would levy charges, but re-invest their profits.

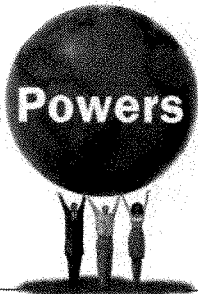
By recent Lib Dem standards, this is pretty bold stuff. Maybe some of the ideas are impractical. It doesn't matter. What does is that on the most important domestic policy issue of the day, the Liberal Democrats now have something to say that is both distinctive and at least superficially attractive. For that, Mr Kennedy deserves some praise. ■

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Mobile telecoms

Time for plan B

A technological escape-hatch exists for Europe's troubled mobile operators. But they are not allowed to use it

AT LAST, some good news for Europe's ailing wireless industry: Mobilkom, an Austrian operator, this week launched its third-generation (3G) service. 3G is faster than existing 2G technology, with the potential to offer whizzy new services such as sending video by phone. Hutchison 3G will launch in Britain next week. Is the 3G bandwagon finally starting to roll?

Well, not quite. In both cases, handsets are in very short supply. Sonera, Finland's national operator, was due to stage its 3G launch on September 26th, but postponed it until next year due to handset shortages. How embarrassing for Sonera, and for Nokia, the world's largest handset maker. The fact that the two firms cannot get 3G to work in their wireless-crazy Finnish homeland does not bode well.

Why the delay? European operators must, under the terms of their 3G licences (for which they paid over €100 billion, or \$90 billion), provide 3G service by particular deadlines, and do so using a technology known as W-CDMA (never mind what the letters stand for). Alas, W-CDMA does not work yet. Handsets made by one firm do not work properly with network equipment made by another, says Björn Krylander of UbiNetics, an equipment-testing company. Since operators prefer to use equipment from more than one supplier, 3G can only take off when this pro-

blem is solved, which could take a while. 3G seems unlikely to become widespread in Europe until 2004 at the earliest—and it will be several years before it turns a profit.

These technical problems, and the resulting delays, have far-reaching consequences. A number of European operators are backing out of their 3G commitments or trying to win concessions from regulators. In July, Sonera abandoned a €9 billion joint venture with Telefonica Moviles, a Spanish operator, to launch 3G services in Germany. Orange, a multinational operator, has asked Sweden's regulator to postpone the 3G-rollout deadline until 2006. Tele2, a Swedish operator, is threatening to abandon its operations in Norway unless the licence terms are eased. And Spanish operators are lobbying for a refund of deposits paid for their 3G licences.

Alphabet soup

Back in the 1990s, the European Commission's decision to impose a single technology standard for second-generation (2G) phones, called GSM, on Europe's operators worked well. It allowed roaming from one country to another, and Europe's wireless firms, notably Nokia and Ericsson, rose to prominence as GSM became the dominant 2G standard worldwide.

Imposing W-CDMA as a single standard in 3G now looks like a big mistake. Far

from reinforcing Europe's leadership in wireless, it has done the opposite. Morgan Stanley recently concluded that Asia now leads the world in the adoption of 3G, followed by America. Europe is last.

That is because as Europe struggles with W-CDMA, a rival 3G technology called CDMA2000 is working well elsewhere. Unlike W-CDMA, which is controlled by a huge industry consortium, CDMA2000 is controlled by a single American company, Qualcomm. Different vendors' equipment is compatible. Over 17m people in South Korea, Japan and America use a version of the standard called CDMA2000-1X (again, never mind). The industry is fiercely divided by a boring technical argument about whether CDMA2000-1X is really 3G or not. But ultimately the argument is irrelevant. CDMA2000-1X can do everything W-CDMA can; more, in fact, since it actually works. It is 3G in practice, even if not everyone agrees that it is 3G in theory.

In Japan, CDMA2000-1X and W-CDMA are competing head to head, and the results make grim reading for European operators. Japan's NTT DoCoMo launched the world's first commercial W-CDMA network in October 2001. Since then, it has signed up a mere 135,000 subscribers, far short of expectations.

Its rival KDDI, in contrast, launched a CDMA2000-1X service in April 2002, and has already signed up 2.3m customers. Half of those subscribers have camera-phones, which they use to zap pictures over the airwaves, spending an average of \$11 per month more than subscribers with ordinary phones. DoCoMo's average monthly revenue from its 3G subscribers, meanwhile, is falling, the battery life of its 3G handsets is poor, and subscribers have ▶▶

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► to carry two phones if they want to stay in touch outside areas of 3G coverage.

No wonder operators everywhere that had planned to adopt W-CDMA are thinking again. The industry's consensus that W-CDMA will eventually grab 80% of the world market for 3G, and CDMA2000 just 20%, is being re-evaluated.

In South America, operators have abandoned or frozen plans to adopt W-CDMA. Telstra, in Australia, is leaning towards CDMA2000. Most important of all, in China, the world's largest mobile market, executives from China Mobile have given W-CDMA only a half-hearted endorsement. Adoption of the technology depends on it working properly, the company says, so a switch to CDMA2000 cannot be ruled out. "The question is, should you use the technology that is running today, or wait for one that may or may not run tomorrow?", asks David Chamberlain, an analyst at Probe Research.

European operators, however, have no choice. At least one operator has established a task force to evaluate switching to CDMA2000, says Andrew Cole of Adventis, a telecoms consultancy, and others are no doubt doing the same. But as things stand, says Caroline Easter, a technology lawyer at Ashurst Morris Crisp, Europe's 3G licences are technology-specific, and any firm that adopted CDMA2000 would be in breach of the licence terms.

Even suggesting such a switch in public would have a dramatic effect on European equipment makers, which have signed lucrative contracts to supply operators with W-CDMA network equipment. Tellingly, however, a consortium of eight equipment makers—including Ericsson, Lucent, Nortel and Motorola—recently agreed to co-operate on building CDMA2000 equipment suitable for the European market.

It is not just the imposition of a single technology standard that should be reconsidered by regulators, argues Joe Nordgaard of Spectral Advantage, a consultancy. European operators are also barred from buying and selling their licences—they must simply give them back, with no refund, if they choose to abandon 3G.

Operators also have to adopt 3G in a new frequency band, rather than phase it in alongside existing 2G, as operators are doing with CDMA2000 elsewhere. But these market distortions, says Mr Nordgaard, "can be alleviated to some extent by allowing operators more freedom."

Even if operators wanted it, however, Europe's regulators are unlikely to change the rules, even as they amend licence terms to extend 3G rollout deadlines. Defending the original policy, it seems, matters more than providing consumers and operators with a choice of technologies. Things might have been very different had Europe's operators not been trussed up in a technological straitjacket. ■

Disney

Wobbly kingdom

Disney needs a managerial lion king

HAVING survived this week's board meeting, Michael Eisner, the head of Disney, is a rarity: the boss of a struggling media group still clinging on at the top. But the pressure on him is intense. Investors are disgruntled. Even certain members of the eccentric, usually docile Disney board—which includes a Hollywood actor, a priest and a specialist in early education—are grumbling about his failure to revive the Magic Kingdom. A list of possible successors—from Peter Chernin to Mel Karmazin, seconds-in-command at News Corporation and Viacom respectively—continues to swirl around Hollywood.

What has happened to Mr Eisner, at the helm now for nearly 18 years? Once upon a time he was lauded for the vision and iron grip with which he transformed a business that had become heavily concentrated on its theme parks, with only a small film studio, into a diversified global media conglomerate. Now he is increasingly perceived as a liability. No part of the Disney empire is insulated against trouble.

Through its theme parks, the company has been battered by the downturn in tourism. Its film studio has been boosted by last week's release on DVD and video of "Monsters Inc", an animated film which sold 5m units in one day, a new record. But it has yet to recapture the creative touch which, in the early 1990s, delivered it animated hits such as "The Lion King". Recently, Disney has relied for its creative energy on a partnership with Pixar, which created "Monsters Inc". This venture only lasts for two more animated films. By contrast, Disney's own ability to devise new

children's characters and turn them into classic franchises, branded on to lunch boxes, pyjamas and soft toys the world over, has faltered.

By far Disney's biggest current headache, however, is the broadcast network that Mr Eisner bought in 1996: ABC. Two years ago, when ABC topped the prime-time ratings league with "Who wants to be a millionaire?", a quiz show, the network was throwing handsome profits into the Disney pot. In the nine months to June 2000, operating profit at ABC topped \$1 billion, nearly one-third of the group's \$3.2 billion total. In the nine months to June this year, however, ABC made a pro forma operating loss of \$13m, dragging down the company's operating profit to \$2.3 billion.

Part of ABC's problem is the advertising slump, which has especially hurt the network since it slipped from top of the prime-time ratings to third place this year, behind NBC and CBS. But ABC also faces a particular challenge. The other networks launched their new TV shows this week on the back of established hits returning for another season. ABC has none, having so over-exposed "Millionaire" that it bores even America's couch potatoes.

Earlier this year Mr Eisner fired Stu Bloomberg and installed Susan Lyne as head of ABC Entertainment. He also recruited Steve Sohmer, a TV veteran, to overhaul ABC's marketing. Every part of Disney, from theme parks to cable channels, has been put to work promoting the new TV shows.

Early reactions to two new ABC sitcoms, "Eight simple rules for dating my teenage daughter" (see photo) and "Life with Bonnie", are promising. Each topped the ratings in their time slots. But other new ABC series are going head-to-head with old favourites on rival networks, such as "Friends" on NBC, which this week won an Emmy award for best comedy. And even if ABC can conjure up one or two new hits this season, that still may not be enough to reverse its fortunes. "It typically takes two to three years for a network to pull itself up," comments Christopher Dixon, a media analyst at UBS Warburg, an investment bank.

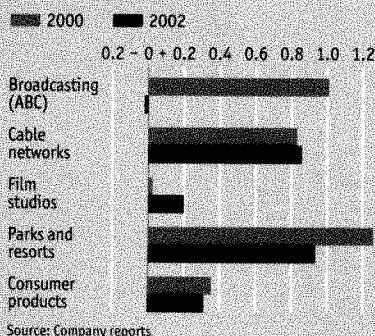
More tricky still, Disney bears most of the risk involved in new shows, because most of those it is launching on ABC this season have been made by the Disney-owned TV production studio, Touchstone Television. By industry standards, this ►►



Michael Eisner's lucky number?

Missing magic

Disney, operating profit/loss by sector
nine months to June 30th, \$bn



► model is not unorthodox. Viacom's CBS and News Corp's Fox, two other networks, belong to media conglomerates, each also relying on a sister studio to feed much of its programming. This lets the network, and its giant owner, capture more of the long-term value of shows once they are hits.

The downside is that the network does not share development costs for new shows with an outside partner. And it relies on the creativity of the parent's in-house studio. Given Disney's corporate instinct to control creative ideas, an urge embodied by Mr Eisner, an English literature and theatre graduate who has never hidden his preference for the creative side, pushing the own-label model to its limits may have been counter-productive.

Recently, ABC and its Disney parent have begun to recognise the limits of this do-it-yourself model. Of its new shows in development, to air in a year's time, only about half are being made in-house, down from 86% of this year's debutants. "I've been aggressive in going out and telling all the studios we're open for business," says Ms Lyne, "No one studio can deliver all the programming a network needs."

ABC is exploring other changes. Last month it signed a programming deal with HBO, a premium cable channel behind the hit comedy "Sex and the City" and such classy dramas as "Six Feet Under" and "The Sopranos". HBO is owned by AOL Time Warner—and Disney is also talking to that rival media giant about a cost-cutting joint venture to merge CNN, a cable news channel, with ABC's broadcast news.

Plainly, Mr Eisner would not have hired Ms Lyne had he not approved of the idea of fishing in a wider Hollywood creative pool. To that extent, he is prepared to let go, at least a little. "It's ridiculous to think that Michael would be reading scripts and watching rough-cuts," insists Ms Lyne. Maybe so. Yet a tension remains. Mr Eisner could not resist sitting in on discussions about scheduling for this season, and which shows the network should broadcast. If ABC fails to pull off a revival, he will have nobody to blame but himself. ■

Vivendi Universal

Plus ça change

Whither France's global media dream?

THERE was one irony, and few surprises, in the strategy for Vivendi Universal announced on September 25th by Jean-René Fourtou, its boss since July. Mr Fourtou was drafted in to rescue Vivendi from bankruptcy after Jean-Marie Messier left in disgrace, having chased a financially reckless dream of turning a dull French utility into a global multimedia giant. So would Mr Fourtou return the company to its French roots based in utilities? Not a bit of it. "Vivendi Universal is basically an entertainment company," he declared. It will keep its American film studios, music and television assets, run by Barry Diller, after all.

This irony might make strategic sense were Mr Fourtou clear about his plans for the non-media assets. Yet he insisted he had no wish either to raise or reduce Vivendi's 41% stake in Vivendi Environnement, a utilities firm. He would not make clear any plans for Vivendi's minority stake in Cegetel, the majority owner of SFR, a cash-generating mobile operator. Without control of Cegetel, Vivendi cannot get its hands on that cash. A fight to boost its stake would pit Vivendi against mighty Vodafone, a telecoms firm and Cegetel shareholder.

That left a less glittering list of assets to be shed to pay down Vivendi's €19 billion (\$18.6 billion) net debt. Mr Fourtou promised to raise €12 billion from asset sales by December 2003; €5 billion of them by next March. The big prize is

Vivendi's publishing unit. Some bids are already in, and the sale might bring in around €3.5 billion. Mr Fourtou also announced the sale of Telepiu, a cash-draining Italian pay-TV operator, to Rupert Murdoch's News Corporation for €1 billion, two-thirds of the price discussed a year ago. A minority stake in Vivendi's games unit will be "monetised", possibly via a separate listing.

The rest must come from smaller assets, such as Canal Plus's foreign units and Messier-era extravaganzas such as corporate jets and flashy property. Last month, Vivendi sold Vizzavi, an Internet portal, to Vodafone for €143m. This week it sold Canal Plus Technologies to Thomson Multimedia for €190m.

Mr Fourtou is treading a perilous line between his creditors' need for cash and his investors' hunger for strategic clarity. He does not want to make any fire-sales. Yet, as he admitted, even with the €3 billion medium-term credit line he secured last week, replacing an earlier €1 billion loan, the liquidity crisis "is not perhaps behind us, but is being resolved".

Mr Fourtou's plans underline the collapse of the idea of "convergence" in the media industry. Telecoms, regarded by Mr Messier as the centrepiece of his vision of marrying old and new media, is now just a cash cow; Vivendi's Internet units a cash drain. Mr Fourtou may still have to prove what his strategic vision is; but it is quite plain what it is not.

Drug side-effects

Pain killer

NEW YORK

Its maker may finally have to admit that Tylenol can be a dangerous drug

AFTER 25 years of study, a Food and Drug Administration (FDA) advisory panel decided last week to recommend that acetaminophen, the active ingredient in Tylenol, America's most popular non-prescription drug, should carry an explicit warning about potential liver damage. "You cannot allow more innocent men, women and children to suffer," said Kate Trunk at the FDA hearing before the advisory panel's vote. Her son recently died from liver disease after taking an acetaminophen drug after injuring his wrist.

Even the possibility that a problem ex-

ists in acetaminophen came as a shock to many Americans, 55m of whom use Tylenol each year. Johnson & Johnson (J&J), a big drugs company, made Tylenol into a huge success with an advertising campaign boasting, "nothing's safer". The reputation of product and firm were intertwined in 1982 when J&J immediately responded to a tampering incident that cost seven lives, recalling every package. The incident became the most famous case study in corporate social responsibility.

But while J&J was quick to address external threats to Tylenol, it only grudgingly faced up to problems with acetaminophen itself. The distinction between a safe and a harmful dosage is particularly narrow and it can be toxic in relatively small quantities. According to documents that emerged in lawsuits, J&J was aware that explicit health warnings would damage Tylenol sales. Perhaps not coincidentally, its labels in most cases bear no reference to the potential harm in taking acetaminophen. ►►



Nothing's safer?

Each year there are 56,000 emergency-room visits because of acetaminophen overdoses, and 100 fatalities, says the FDA. According to William Lee of the University of Texas Southwestern Medical Centre, acetaminophen is the leading cause of acute liver failure. In a recent FDA study of patients with liver damage linked to acetaminophen, 20% had used less than the recommended daily dosage.

Yet Tylenol-related lawsuits have rarely succeeded. It is difficult to link cause and effect definitively in a medical case. Many people use the drug without problems. Often, J&J has in effect argued that the victim could not prove that the recommended dose had been precisely followed. Even so, in 1994, it lost a \$9m verdict to Antonio Benedi, whose liver was destroyed by Tylenol. Mr Benedi had taken it as directed, along with a little wine.

Soon after, J&J started to include a vague warning with each adult Tylenol package, noting that liver damage could result when the drug was mixed with alcohol. It did not explicitly warn consumers that liver damage was possible from taking Tylenol even without alcohol.

An FDA panel first proposed requiring a warning linking acetaminophen to liver damage in 1977. It did so again in 1988 and 1993. Most of the data used by the FDA in making its recommendation, it concedes, has long been known. For the warnings to become mandatory, the FDA must formally adopt the recommendation, and it may face lobbying like that which stymied past attempts. This week a new boss was nominated for the FDA, Mark McClellan, an economist on the Council of Economic Advisers. For insight into the opportunity costs of bureaucratic delay, Ms Trunk would be a good person for Mr McClellan to consult. Sadly, she is not alone. ■

Doing business in Zimbabwe

Aasvoels circling

HARARE AND JOHANNESBURG

Vultures are eyeing Zimbabwe's firms

IF THE best time to invest is when blood is in the streets, Zimbabwe offers a promising opportunity. The country is in the throes of political upheaval, with 6m hungry people, an inflation rate of 135% and a shrinking economy. The rule of law is collapsing. Judges are routinely intimidated. The government sends thugs to grab commercial farms. And fears are growing of much worse civil strife to come.

Enter the bargain hunters—call them aasvoels, Afrikaans for vultures. Zimbabwe boasts vast quantities of valuable minerals, including one of the world's largest deposits of platinum. South Africa's Impala Platinum recently upped its shareholding to take effective control of Zimbabwe Platinum Mines. It has also increased its stake in a smaller platinum company, Mimosa. Platinum sells for \$574 an ounce,

and the low costs of mining it in Zimbabwe mean that both ventures are too tempting to pass up, despite the political risk, says Keith Rumble, Impala's boss.

Zimbabwe's fuel and energy shortages are also tempting outsiders. President Robert Mugabe's Libyan allies have just renewed an annual \$360m deal to cover most of the costs of importing oil. The Libyan government will get assets once owned by the Zimbabwean state, including 14% of Jewel Bank and 14% in Rainbow, a tourism group, and maybe some land. Talks are said to be under way to give Libya control of fuel tanks in Harare and a strategically vital oil pipeline linking Zimbabwe to a port in Mozambique.

Eskom, South Africa's energy utility, the world's fifth biggest, is eyeing Zimbabwe's energy giant, Zesa, which is slated to ►►

Accounting scandals

Worthless promises?

NEW YORK

Was American bosses' first certification of accounts a non-event?

REMEMBER the fuss around August 14th, the date by which America's corporate chieftains had to swear personally to the accuracy of their companies' accounts, under orders from the Securities and Exchange Commission (SEC)? This was supposed to restore the confidence of investors, savaged by accounting scandals from Enron to WorldCom. Certification, carrying with it the prospect of criminal prosecution for the signatories if the accounts later proved to be fraudulent, would presumably not be done lightly. Bosses hated the idea, and spent small fortunes on legal advice.

It was widely believed that certification would boost the share price of those firms whose bosses signed, while hurting those whose bosses declined to do so. What actually happened is the subject of a new study by Utpal Bhattacharya, Peter Groznik and Bruce Haslem of the Kelley School of Business at Indiana University. They examined the share prices of 762 firms, 688 of which had to certify by August 14th and 74 that certified voluntarily, seeking out any impact of certification or non-certification.

They found crucial differences between the 738 firms that provided a pro-

forma certification, the 15 that certified using their own words and caveats, and the nine that failed to certify at all. The nine tended to be firms that had restated their accounts in the previous year, were financially distressed, had a relatively low proportion of institutional shareholders and were audited by, you guessed it, Andersen.

But on the crucial question of its impact on the stockmarket, they found that, on average, announcing that a firm had or, more strikingly, had not certified made no significant difference to its share price. The likeliest explanation for this, say the three economists, is that the market was not in the least bit surprised by those firms that stood by their accounts and those that did not. Indeed, the study suggests, share-price movements indicate that the market had sorted out the corporate sheep from the goats by April 2002, well before the SEC made its certification order in June.

Or perhaps investors had so lost faith in CEOs that they dismissed their signatures as empty pledges not worth the paper they were written on. Whatever, says Mr Bhattacharya, certification seems to have been "a non-event".

be privatised. Zesa is far short of the \$200m or so in hard currency it needs each year to pay for equipment and to service debts accrued to Eskom, which supplies electricity to Zimbabwe's grid. The South African supplier may hope eventually to swap debts for a share in the Zimbabwean company, and is building a close partnership. Zesa is increasingly reliant on the support of its South African big brother.

Most South African companies are understandably wary of doing business in Zimbabwe—until recently South Africa's biggest African trading partner but now down to third place. Anglo American is reducing its investment in its citrus and timber estates there, though it plans to retain its much more lucrative mining interests.

Other large trading firms still see opportunities. Last year Barloworld bought a Zimbabwean cement and lime producer. South African Breweries is keeping its 25% stake in Delta, a beverage company. "There is huge consumer spending power in this market for trading companies. Often people here have money for goods, but nothing to buy," says John Robertson, an independent economist in Harare.

The World Food Programme expects to spend one-fifth of its \$500m food budget on transporting grain within the region, about half of it in Zimbabwe. Private-sector haulage firms, many of them South African, charge up to \$90 for every tonne shifted. Other private traders are finding original ways to get goods to Zimbabwean consumers. Two online firms, Sadza.com and Emoneytransport.com, let well-wishers overseas send money and food to relatives in Zimbabwe via local supermarkets. The situation is desperate for most, but a few firms may have reason to smile. ■



Business is for the birds

An innovative Japanese restaurant chain

Food for thought

TOKYO

Global Dining is revolutionising Japanese work practices

TRADITIONAL *ryotei*, where elegant kimono-clad women serve dainty dishes and fragrant sake, are usually the dining spots of choice for foreign heads of state visiting Tokyo. But when George Bush arrived earlier this year, Junichiro Koizumi, the prime minister, took the American president to Gonpachi, a huge, trendy tavern in Tokyo's hottest night spot. In contrast to the discreet formality of *ryotei*, the bustling, occasionally raucous Gonpachi, decorated with fat sake kegs and strings of paper lanterns, suited Mr Koizumi's populist image and helped to show off an easy bond with his buddy, Mr Bush.

The visit was a huge feather in the cap of Kozo Hasegawa, the maverick founder of Global Dining, which owns Gonpachi and a string of other popular restaurants, including a couple in California opened as a pilot for a possible global expansion.

Global Dining restaurants offer decent food at a reasonable price and stay open late. The restaurants have funky themes, ranging from the Gothic splendour of *Tableaux*, which offers Californian cuisine, to its latest venture, the disco-style *Dancing Monkey*, complete with glittering mirrored balls and zebra-patterned floors.

But Global Dining's greatest strength is its efficient and attentive service, fostered by vigorously defying traditional Japanese business practices. A decade after Global Dining started life as a coffee shop in 1973, Mr Hasegawa concluded that its conventional Japanese seniority system bred complacency, causing his restaurants to lose customers and money. Now the firm, which has annual sales of ¥11.7 billion (\$98m), boasts a competitive system of carrots and sticks for workers that might shock even ruthless American employers.

Most of the 1,400 staff are hired first as part-timers, mostly in their 20s and on minimum pay. To get a raise, they must win the backing of a majority of their co-workers at one of the regular staff meetings. A thick skin is essential, as colleagues tend to be blunt in their discussion of strengths and weaknesses. Applicants take criticism—which has been known to address subjects such as overly-strong body odour—in their stride. So much for the traditional Japanese workplace, full of passive workers strenuously avoiding confrontation and personal accountability.

Life gets no easier higher up the ladder. Increasing sales, a restaurant manager's top priority, is tough given the sagging

economy. Poor performance leads to demotion, while the successful are rewarded just as swiftly. Naonobu Takashima, the 25-year-old manager of *La Bohème*—themed as a medieval European castle—was hired as a part-time waiter in March 2001 on ¥850 (\$7) an hour. Six months later, he was put in charge of one of Global Dining's leading outlets. He now earns around ¥15m a year, a rapid seven-fold increase perhaps unprecedented in Japan.

Global Dining's culture is winning influential admirers. Some senior executives at blue-chip firms are so impressed that they are sending their offspring to be trained at the restaurant chain.

After a TV programme on Mr Takashima's meteoric rise, busloads of restaurateurs from across Japan started visiting *La Bohème* to watch the young star in action. There have been some typically Japanese side-effects. Some traditional businessmen, who spent decades climbing the corporate ladder, found his rapid success hard to accept and abused him on the firm's website. He was even heckled at work.

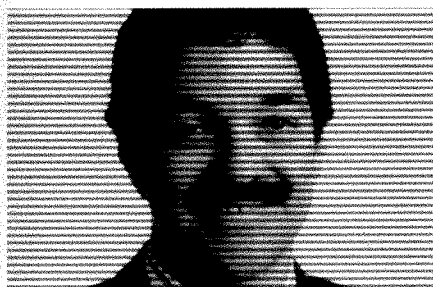
Global Dining's meritocracy has forged an army of highly professional workers, trained to make wide-ranging decisions on how a restaurant should be run. They are tempting recruits for rivals. Even Global Dining's drop-outs are mostly considered better than average industry workers and are soon hired elsewhere.

There was a huge exodus after Global Dining went public in 1999. A quarter of its managers cashed in share options and left to start their own restaurants. Not only did it lose some of its stars—some of them also became its fiercest competitors. Global Dining's share price has plunged by 90% since listing its shares. Analysts say the main problem, apart from a market-wide collapse in share prices, is its failure so far to nurture a big batch of new talent.

Mr Hasegawa agrees and is searching for ways to keep the best of the current workforce. One idea is to let them come up with—and execute—concepts for new restaurants. That way, he says, they can enjoy much of the freedom and excitement of starting a business themselves, but with a financial safety net and a ready-made pool of good staff. Perhaps quite soon, an even bigger prize will be on offer. Unusually in a country that prefers to keep businesses in the family, the 52-year-old Mr Hasegawa says his own job will be up for grabs in an open competition when he retires. ■

Face value Ex-friends of Frank

If being a friend of Frank Quattrone was wrong, how should company bosses relate to their bankers?



AMERICA today is not short of corporate scallywags. But historians may reserve a special place in the crowded gallery of rogues for Frank Quattrone. Mr Quattrone was an investment banker who wheeled and dealt his way through the 1990s and a string of ever-more-generous employers to fame and fortune. But what really marked him out were his social talents. Mr Quattrone was a very friendly man.

He had an apparently straightforward approach to making friends. His job was to find technology firms for his employers to sell via initial public offerings (IPOs) of shares. At 7% of the money raised, IPO fees are famously good business. Most of the newly issued shares, which typically soared in value on their first day of trading, went to the big investing institutions. But at Credit Suisse First Boston (CSFB), Mr Quattrone's employer since 1998, a few IPO crumbs fell into the laps of the brokers who worked alongside him. These brokers reportedly ran what were dubbed "Friends of Frank" accounts, opened on behalf of executives of valued tech-company and venture-capital clients that Mr Quattrone hoped to befriend. Into these accounts went the fresh IPO shares. Then, once they had risen nicely, CSFB's brokers would "flip" or "spin" them to less fortunate buyers, booking the profits for Frank's friends—a business gift, as they say in Saudi Arabia.

Like much of what passed as industry practice during the late 1990s, spinning is now under investigation by everyone from securities regulators to Congress. Already, besides CSFB, these investigations embrace Citigroup (owner of Salomon Smith Barney), Goldman Sachs and others. The wickedness of Wall Street's bankers no longer surprises.

More intriguing is the behaviour of those chief executives, chief financial officers and others who took these gifts from Mr Quattrone and his ilk. It was their

clear duty to get the best possible deal for their shareholders. Yet new issues were routinely priced far below the market-clearing price. It now seems not unreasonable to think that many managers may have tolerated these practices for personal gain.

Time was, seasoned investment bankers will tell you, that this sort of relationship between a company and its banking advisers could not have existed. No-one can exactly date this golden age of banking, though some wistfully recall the era of John Whitehead and John Weinberg at Goldman Sachs, especially in the 1970s when that firm was in its prime. In this age, before the fall, strode men of professional integrity and moral clarity, dispensing, if need be, the icy blast of truth to their clients. Well, that's the story.

Sin comes to Wall Street

Then came the fall. In 1975, fixed trading commissions ended, and competition and deregulation were let loose. Financial innovation thrived, creating huge opportunities for making money. New markets arose in mortgage-backed securities, junk bonds and leveraged buy-outs. Providing professional, independent advice suddenly looked like a poor man's game.

The monthly retainer withered away and banks began demanding a percentage of the deal. At a stroke, they lost their ability to provide impartial advice: the overwhelming incentive was to close the deal almost regardless. But as the markets in mergers and IPOs boomed, the rewards looked worth it.

Some captains of industry were terrified by this new, barbarian-filled world of finance. Others quickly came to understand its logic. Bankers could never be trusted to give impartial advice. But when opportunity for mutual benefit arose, they could become your partners.

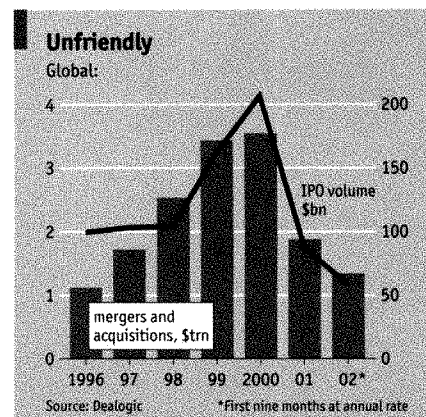
As the great bull market of the 1990s rumbled on, the partnerships deepened. When corporate bosses berated their bankers for unenthusiastic research reports by their analysts, those analysts jumped. Eager to close the latest deal, bankers massaged egos, playing to the strong sense of hubris in America's boardrooms. Jack Grubman, a Salomon Smith Barney star analyst, even sat in on board meetings at WorldCom, a deeply corrupt telecoms firm, offering advice. Looking after the boss with hot IPO stocks, as Mr Quattrone and others did,

symbolised and sealed the partnership between bank and company.

The problem, of course, is that independent advice can sometimes prove priceless. Who was there to caution against the mad stampede of telecoms firms into fibre-optic cable? Or that miserable marriage of old and new media in the merger of AOL and Time Warner? "Hardly anyone was fairly compensated to work on the other side of the market," says Charles Ellis, the founder of Greenwich Associates, a research firm. "Everyone's interests were the same."

The market's collapse has brought this game to a jarring halt. From 2000 to 2001, merger volumes halved. This year, they will fall again. There are good deals to be done—in the telecoms industry, for instance, which needs consolidating. But any banker proposing one is likely to get short shrift from today's bosses, ever mindful of their suddenly suspicious board members. Today, no investment banker can be trusted. Where are Frank's erstwhile friends now?

So, have bosses regained their appetite for independent counsel? And if so, who will provide it? Investment banks must wrestle with the huge cyclicity, conflicts of interest and brand damage that their past choices have bequeathed them. Perhaps new leaders will make better choices. But the risk is that the banks will fall apart under their conflicts of interest, replaced by advisory banking boutiques or management consultants. While the rewards for advising on deals remain large, however, genuine independence may prove elusive. Bosses should remember Mr Quattrone next time some hired hand urges them to issue securities or merge. Beware advisers bearing gifts. ■





Doubts inside the barricades

WASHINGTON, DC

It is not just anti-globalisation protesters who are wondering whether the IMF knows what it is doing

THE International Monetary Fund (IMF) and the World Bank will again be under siege this weekend. Thousands of anti-globalisation protesters intend to encircle the organisations' Washington headquarters—where finance ministers and central bankers from 184 countries hold their annual meetings on September 28th and 29th—in order to save the world from the “economic smallpox” inside. After a brief lull in the wake of last year's terrorist attacks, the travelling circus of anarchists, students and activists, who try to wreck international economic meetings with what they call “creative confrontational opposition to capitalism”, is back.

Though these banner-wavers hog the headlines and disrupt the streets, they pose no serious threat to the two Bretton Woods institutions. Their goals (such as “end capitalism”) are too absurd; their arguments too incoherent. But this year, more than most, the IMF faces criticism from a more serious source—those inside rather than outside the barricades. A growing chorus of insiders, from staff members (sotto voce) to Wall Street bankers (more loudly), is asking whether the Fund and the rich countries that largely determine its

policies know what they are doing.

The reason for the current disquiet is Latin America. A region that was only recently the darling among emerging markets now includes several countries that sit on the edge of financial disaster. Argentina has already fallen into the abyss. Its default on its external debt triggered an economic depression without parallel there since the 1930s. Its economy could shrink by more than 15% this year.

The collapse has dragged down Uruguay, Argentina's next-door neighbour, a country whose debt long held a prestigious investment-grade rating. An American bridging loan and an IMF bail-out averted a banking crisis there in August, but most observers—and, privately, even economists at the IMF—say it is a matter of when, not if, Uruguay defaults.

Now uncertainty about the outcome of its presidential election in October has pushed even Brazil, the region's giant, to the wall (see page 73). A pre-election financial catastrophe was staved off only by a \$30 billion IMF loan in August, the organisation's biggest ever. Elsewhere, Paraguay has turned to the Fund for the first time since the 1960s, and Ecuador and Co-

lombia are both in trouble. Chile and Mexico are the sole bright spots in a region whose GDP, according to some forecasters, will shrink by around 1% this year.

Most countries in the region have been squeezed out of the international capital markets. The interest-rate spread between US treasury bonds and the average Latin American bond is over 1,200 basis points, or 12 percentage points, almost double the spread earlier this year (see chart 1 on next page). According to the Institute of International Finance, Latin America will see only \$29 billion of net private capital inflows this year, compared with \$45 billion last year and \$106 billion five years ago (see chart 2 on next page).

For the IMF, Latin America's current plight is the latest disaster in a litany of emerging-market crises over the past decade—from Mexico's currency crisis in 1994-95 to the Asian financial crises of 1997-98 and Russia's default in 1998. Cumulatively these have already deeply dented the organisation's credibility as a font of good economic advice. The Fund's main explanation for previous mistakes—that it was practising “battlefield medicine”—is less credible this time round. In Asia, it had to decide quickly how to cope with sudden exchange-rate crises in countries with which it had not been closely involved for years. In Russia, it was assisting in an unprecedented switch from communism to capitalism. In both cases, mistakes were to be expected. Latin America, in contrast, is a region in which the IMF has been immersed for decades.

In the 1990s, in particular, it was mid-►

► wife to the region's embrace of economic reform—of the deregulation, liberalisation and privatisation that make up the so-called “Washington Consensus” of policies for emerging-market prosperity. Latin American countries slashed trade barriers, sold off state assets, and opened their financial systems to foreign capital. Given the Fund's close involvement, even Horst Köhler, the IMF's boss, recently admitted that the failure to avoid the current turmoil “suggests that we still have a lot to learn”.

Consensus objectors

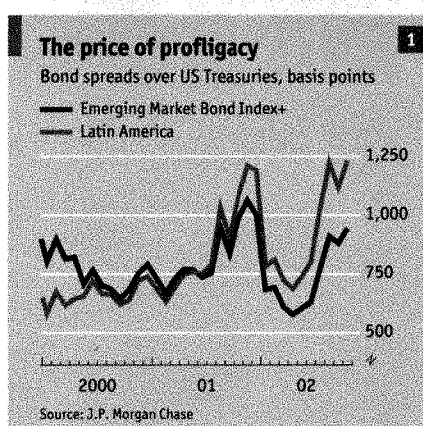
What should these lessons be? The criticisms of the IMF are numerous and not always consistent, but three big themes stand out. One line of argument blames the current turmoil on Latin America's failure to adopt the Washington Consensus with sufficient rigour. Ernesto Zedillo, Mexico's former president, for instance, wrote recently in *Forbes* magazine that the region suffered from too little reform rather than too much.

It has become conventional wisdom in recent years that sustainable growth in Latin America demands more than liberalisation and privatisation. Deeper structural change—from improving education to overhauling judicial systems—is necessary. But, this analysis suggests, disciplined policies are a prerequisite. The lesson is that the Fund must become tougher.

A second line of argument suggests that parts of the Washington Consensus itself are to blame: that the Fund pushed countries into opening up their economies to foreign capital prematurely, and that this openness lies at the heart of the current turmoil. In its extreme form, this critique is often associated with Joseph Stiglitz, a former chief economist at the World Bank and author of a recent book which denounces the IMF as the ideological handmaiden of Wall Street. While few insiders agree with Mr Stiglitz's analysis, there is a growing disquiet even among the IMF's own economists about the risks involved in foreign capital flows, particularly the debt finance that many Latin American countries have binged on recently.

The third set of criticisms, offered mainly by Wall Street financiers and others who have lent to emerging markets, blames the IMF and its political masters, especially America, for inconsistency. During the Clinton years, countries that faced financial crises were given large IMF loans in exchange for tough policy reforms. But the Bush administration was determined to change this, worried that a culture of bail-outs led investors to reckless lending. Thus Argentina was eventually left to default in December 2001.

Since then, however, the IMF has actually given huge financial packages to Brazil and Turkey even as Paul O'Neill, America's treasury secretary, has decried bail-outs.



According to many in the private sector, this inconsistency, coupled with the absence of any real American engagement in Latin America, lies behind much of the recent trouble.

Silence and the damned

There is some truth in all of these criticisms. Despite the hype of Latin America as a model pupil, a lot of important reforms did not get done during the boom years of the early 1990s. In particular, governments continued to spend too much. Though budget deficits seemed under control, the reality was invariably less rosy. Too often, the cash that came from large-scale privatisation was used to avoid tough budget choices.

In a recent book, Michael Mussa, the head of the IMF's research department until summer 2001, analyses this process in Argentina's case. (“Argentina and the Fund: From Triumph to Tragedy”, published by the Institute for International Economics.) Mr Mussa points out that for all Argentina's spectacular successes (such as its quashing of hyperinflation), the country never got its fiscal accounts in order. Between 1993 and 1998, when the Argentine economy was growing at an average of 4.4% a year, the ratio of public debt to GDP rose sharply from 29% to 41%.

Government profligacy, particularly in the mid-1990s, spawned the debt problem that sank the Argentine economy last

year—and the IMF failed to stop it. Although the Fund's economists would complain about the budgets privately to the Argentines, the Fund never publicly made a fuss or halted a loan programme. One reason for this spinelessness, Mr Mussa argues, is that the Fund's economists got too close to their clients.

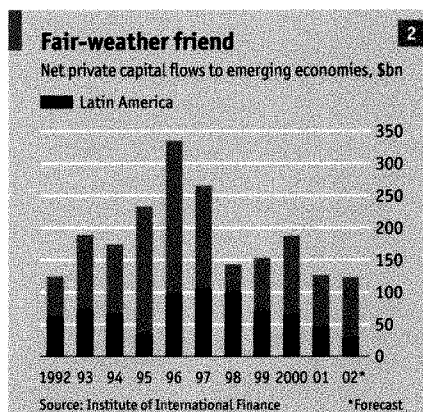
Mr Mussa's critique has clearly resonated inside the IMF. Claudio Loser, an Argentine economist and long-time boss of the Latin America department, has been booted out, along with a number of his key staff. He has been replaced by Anoop Singh, an Indian who speaks little Spanish and no Portuguese, and whose most recent big assignment was in dealing with Indonesia's problems. Mr Singh's instructions from the top are clear: find a new way of dealing with Latin America.

Shuffling the staff may help the Fund become, or at least appear, tougher. But the truth is that when financial markets are pouring money into a country, it is hard for the IMF to have much clout. In the good times, it is often sidelined: Brazil, for instance, had no loan programme with the Fund as its debt burden began to soar in the mid-1990s. And even when the Fund is around, it is easier to ignore. In 1997 and 1998, exactly when Mr Mussa argues that the IMF should have been tougher, Argentina was a darling of emerging-market bond investors. Even if the IMF had blown a whistle loudly, it is hard to believe that it would have made much difference.

The volatility of portfolio finance—its tendency to pour in when investors are confident, and flee just as suddenly—is the main reason for growing scepticism about the whole process of foreign borrowing by emerging-market economies. Each of the debt crises of the past decade has taught lessons; in particular, the danger of a pegged exchange rate. But Brazil's current turmoil shows that even countries that appear to do everything right, can suddenly get into trouble.

Brazil has a big debt burden, the relic of inadequate fiscal discipline in the mid-1990s and failed efforts to defend an exchange-rate peg in 1999. But it is a burden that few bondholders worried about until early this year. Moreover, since 1999 Brazil has had exemplary economic management. Its exchange rate floats; its banking system is strong; and it has run a budget surplus (excluding interest payments) of over 3% of GDP. Yet, earlier this summer, concerns about the outcome of October's presidential election, and sudden jitters about the country's ability to sustain its level of debt, sent real interest rates into double digits and raised the risk of default.

For some critics, Brazil's predicament is a sign that the system is broken. Dani Rodrik, a professor at Harvard University, says it shows that the Washington Consensus model “has run out of excuses”. He ar- ►►



gues that anyone "who still thinks this is an efficient system for resource transfer is mad." Few others go that far, but the cumulative impact of the emerging-market financial crises of the past decade suggests that foreign-currency denominated debt, borrowed in any quantity, whether by the private sector or the government, is dangerous. While many academics, including Ken Rogoff, who replaced Mr Mussa as the IMF's head of research, were warning of the dangers of debt finance in the 1980s, the IMF did little publicly to discourage it during the 1990s.

In Latin America, the failure to sound warnings more loudly is particularly blameworthy. After all, this is a region whose history is littered with surfeits of foreign borrowing. Although the region's debt burden, measured as a share of GDP, is not particularly high (far lower, for instance, than that of countries in emerging Asia), it is extremely high compared with its exports. Latin America's trade integration with the rest of the world is far less advanced than its financial-market integration, partly thanks to rich-country protectionism. And, as a study in the latest IMF *World Economic Outlook* makes clear, countries with deep financial integration but low trade integration are particularly prone to debt crises and currency crashes.

So debt is dangerous, especially in Latin America. But given that many countries have already borrowed up to the hilt, what is to be done? Mr Rodrik argues that the answer is to roll back the clock, give up on the Washington Consensus and reinstate capital controls. Only then, he argues, will Latin America's economies have the breathing space that they need to get any economic growth.

That view is not widely shared. It is becoming conventional wisdom (and indeed IMF policy) that countries which have not opened their financial systems to portfolio capital, such as China and India, should do so slowly and cautiously. But few suggest putting the genie back in the bottle in Latin America, at least not for ever. The region has a long history of capital controls that fostered corruption and were widely evaded. The wealthy simply smuggled their assets abroad, resulting in less investment and growth at home.

A new chapter on bankruptcy?

If debt finance and capital controls are both a bad idea, what is to be done? For now, both the IMF and its political masters are focusing on finding better ways to deal with financial crises. If defaults can be made less destructive, the argument goes, debt is less dangerous.

In November 2001, Anne Krueger, the IMF's number two, floated an idea whose outlines had long been peddled by academics, but never publicly embraced by any international economic officials: that

the world needed the equivalent of a bankruptcy system for countries. The proposal was greeted with scepticism from many governments, and with outrage by investment banks and bondholders, who reckoned it would spell the end of emerging-market debt finance. Few expected the idea to go anywhere at all.

In April this year, Ms Krueger offered a less dramatic version. The Fund's laws should be changed, she argued, to allow a super-majority of creditors to restructure a country's debt. Once such a majority agreed to the terms of a workout, any dissatisfied bondholders would be prevented from challenging it. This arrangement would not legally extend the Fund's power, but it would override current American law, which allows any bondholder to sue for full payment in the event of a default.

In recent weeks, Ms Krueger's plan—called the SDRM (Sovereign Debt Restructuring Mechanism)—has suddenly gained momentum. At their meeting this weekend, the IMF's political masters are likely to ask the Fund to draw up a detailed proposal over the next six months for how to put it into practice.

Does this mean that bankruptcy rather than bail-outs will be the way to deal with all crises? That would be a huge change in the IMF's role. Ms Krueger is less ambitious. She sees the SDRM as a useful tool, one that would help countries whose debt burden was clearly unsustainable (such as Argentina). She imagines the procedure being used perhaps once every three to four years. But in cases where a country faced a liquidity crunch, such as Brazil, the IMF would still need to lend, big time. To drive that point home, Mr Köhler last week suggested that the Fund could need more money in order to be able to deal with capital-account crises.

The Fund's largest shareholder, however, appears to have a different view. The

Bush team's goal is to reduce the need for bail-outs. Mr O'Neill lamented recently that the world faces two uninviting options when a country hits trouble today: "unwarranted lending or sending the troubled nation off a cliff and into a catastrophic default." Privately, the Bush team are quite clear that they want to build a system where emerging markets restructure their debt smoothly and more frequently. Bail-outs are to be minimised.

But to make matters even more complicated, America's actions belie this position. It pushed for the huge bail-out of Turkey, presumably to support a key ally in the war against terrorism. And in Uruguay and Brazil it was keen for the IMF to dole out cash quickly. The generous interpretation of this inconsistency is that the mechanisms for debt restructuring do not yet exist, so bail-outs are an unfortunate, temporary reality. But the truth is that America is hardly rushing to create a better system. Of all the big shareholders of the IMF, America was for long the most hostile to pushing ahead with the SDRM. And America is still loth to develop explicit rules that set limits on how much a country can borrow from the IMF.

Some uncertainty about whether the Fund should push bankruptcy or offer bail-outs is inevitable. Unlike a firm, it is hard to decide whether a country is insolvent or suffering from a market panic. Brazil, for instance, does have a big debt burden. But it is also following tough policies. Nonetheless, the current incoherence over policy is extreme and comes at a particularly dangerous time. The world economy is weak as the excesses of the equity bubble are being unwound. Latin America faces years of hangover from its debt binge of the 1990s. For it to recover without undoing all the other positive aspects of a decade of economic reform will be hard. That the IMF's political masters are adding extra confusion is unforgivable. ■



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Managing Director
Investment Banking

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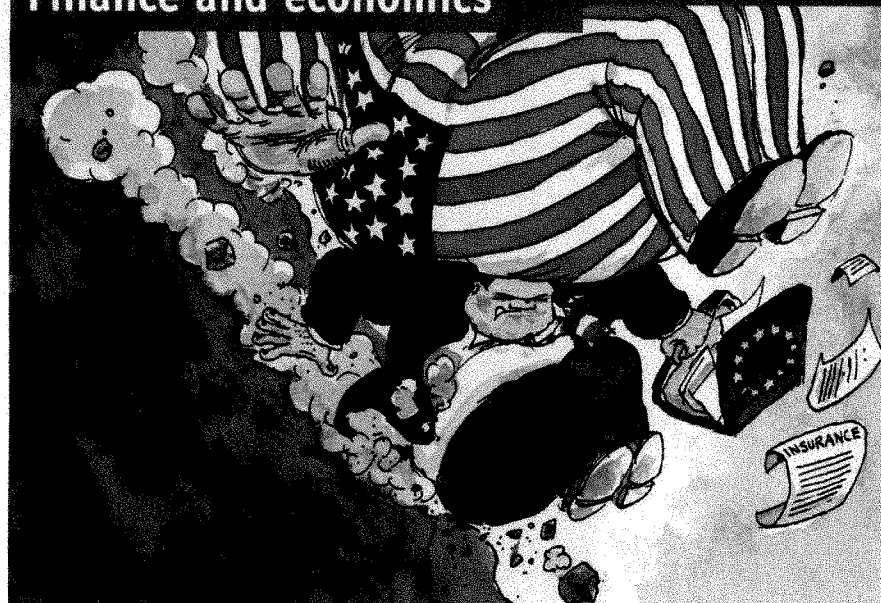
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Europe's tumbling stockmarkets

Feeling for the floor

FRANKFURT

Europe's stockmarkets are suffering even more than America's

AT LAST, on September 25th, some cheer. Despite another wretched economic report—this time, the fourth straight monthly fall in Germany's main index of business confidence—Europe's stockmarkets managed a little rally. Even so, scarcely a dent was made in the balance of the past few weeks, which has been shocking even compared with the feeble performance of American shares.

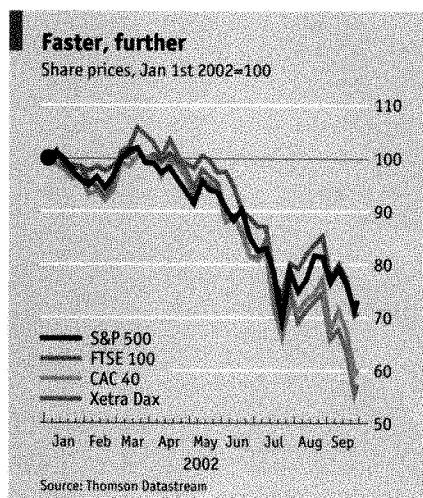
Until mid-July, give or take, Europe's bourses had plotted much the same poor course as America's since the start of 2002, losing one-fifth or so. Since then, American and British share prices have slid, but continental European shares have tumbled. By September 25th, America's S&P 500 had lost 27% this year, much the same as Britain's FTSE 100. France's CAC 40, however, was 40% lower. Germany's Xetra Dax, which this week hit its lowest point since January 1997, was down by 43%.

To be sure, America continues to dominate European markets. Time and again, falls in Europe are reversed if New York traders wake up feeling sprightly. A chirpy mood in the European morning is often spoiled after lunch by bad news from America. In the past few years, the correlation between American and European markets has increased. In the mid-1990s it was perhaps 0.4—with 0.0 meaning no correlation and 1.0 representing total correlation. Lately it has been 0.8-0.9, close to lock-step.

Closer economic ties, driven by huge

investments by European companies in North America, may explain much of this change: one-fifth of corporate Europe's revenues come from North America, says Richard Davidson of Morgan Stanley. On top of this, it seems that correlations among national markets rise during periods of stockmarket boom and bust. When markets were roaring, up to the spring of 2000, investors piled into equities, regardless of nationality. Now they have turned against equities with a similar lack of discrimination.

Still, the latest trouble in European stockmarkets is more than a mere echo—or amplification—of an American tune. For a



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start, European economic growth has disappointed this year, with no sign that the continent is about to take over from America as the world economy's main motor. Economists have been slashing their forecasts accordingly. Europe's less flexible product and labour markets are less well equipped than America's to adjust nimbly in difficult times. Meanwhile, America's Federal Reserve, although it left interest rates alone on September 24th, looks more ready to ward off deflation, if necessary, than does the European Central Bank, which frets still about inflation.

As a proportion of stockmarket capitalisation, the share of telecoms companies—a particularly troubled sector—is twice as big in Europe as it is in America. In Europe, banks and insurers—other sectors under stress—also account for a slightly bigger share of the total market than in the United States. Yet European firms have performed worse than their American counterparts almost across the board. In the past month, the Dow Jones Euro Stoxx indexes have underperformed their American equivalents in 16 out of 18 sectors.

The plight of Europe's insurers adds a special, nasty twist. Typically, 60-70% of British life insurers' assets are in equities, compared with perhaps 20-30% for continentals and almost nil for Americans. Regulations oblige European insurers constantly to mark their portfolios to market—and to offload shares if their value falls too much. Although British regulators have eased these requirements somewhat for the insurers that they oversee, companies have nonetheless been forced to sell shares into a falling market. That has pushed prices down further. The insurers' own share prices have also been dropping dramatically.

Worse still for Europe, says Avinash Persaud of State Street, an American bank, Europe lacks America's "built-in stabilisers". ▶▶

▶ Through mutual funds, for example, America has a certain amount of near-automatic retail demand for shares. It also has a better developed market for corporate bonds, offering institutional investors an alternative to equities. Then there are value investors hunting for bargains. Europe, he reckons, also has contrarians who think that the market is oversold. The regulation of insurers, however, overrides this variety of opinion. "Regulators have yet to learn," he says, "that trying to limit the losses of all the people all the time means there is no one left to buy when markets are going down."

How far are they going? Some strategists believe that after their latest plunge, European markets are at last looking fairly valued, or even cheap. Still, says Nigel Richardson of Axa, a big French insurer, "no one wants to catch a falling knife."

In one respect, though, the dive in share prices has hurt Europeans less than it has hurt Americans. By and large, Europeans have a much lower share of their wealth—especially their pension funds—in the stockmarket. So the knock-on effects of the market crash on consumer spending, and hence on the economy, should be less in Europe than in America.

Less, but perhaps still significant. Meanwhile, there may be longer-term damage, too. Not long ago Europeans, and above all Germans, seemed at last to have been converted to a love of equity, both as an investment and as a way of raising capital. In the past couple of years, falling share prices and rising frauds have taught them the hard way that equity does not mean easy money. A good lesson. Yet it would be a shame if Europe's young equity culture was buried by the market avalanche. ■

cal cycle. An upcoming reshuffle of Junichiro Koizumi's cabinet; the prime minister's rising poll numbers; and rumours that he was growing fed up with Hakuo Yanagisawa, who heads the Financial Services Agency (FSA), the banks' regulator: all this led some central-bank officials to conclude that the odds of Mr Koizumi taking serious steps to restructure bad loans had gone up, and that its extraordinary new policy might push him in the right direction.

With arguments still going on inside the Bank, it is clear that different officials had different reasons for backing the plan, which it was apparently considering weeks in advance. Some, certainly, were concerned that falling stockmarkets risk destabilising the banks, which hold massive equity portfolios that are riddled with losses. With politicians clamouring for the central bank to buy shares, the scheduled replacement next spring of Masaru Hayami, the Bank's governor, also weighed on a few officials' minds. Their calculation seems to have been that it was better to act now, in a fashion that met politicians' approval, than to have an outsider foisted on them. Mr Koizumi has a penchant for appointing private-sector folk to head up public institutions.

Little to date is sure about the share-buying proposals, other than that they will be small—around ¥1 trillion-3 trillion (\$8 billion-24 billion). Indeed, when you compare the surprising break from central-bank orthodoxy with the likely limited impact of the scheme, it does seem more geared towards getting people's attention, and thus allowing the central bank to broadcast its argument. And the argument, quite simply, is that the FSA is failing to deal with the banks' bad loans, amounting probably to ¥150 trillion.

The FSA, just as vehemently, has said that bad loans will soon be coming down nicely, and that better monetary policy would help. The Bank's new contribution to this debate goes something like this: "By doing something that any good central banker would consider nuts, we are showing the prime minister how firmly we believe we are right."

Since they could achieve the same thing by setting their building on fire, why go about it this way? By helping to provide a cushion for banks' share sales, say people at the Bank of Japan, it is providing stability and making it easier for Mr Koizumi to choose decisive action. Unfortunately, the flaw in this argument is that, by the same reasoning, the Bank is also lowering the short-term cost of the government doing nothing about the banks. Every deck in Japan is stacked in favour of muddling through, so the Bank of Japan's gamble thus seems irrationally exuberant. Now that the bet has been taken, the best on-lookers can do is hope that it somehow beats the odds. ■

The Bank of Japan

A great risk, for what reward?

TOKYO

The Bank of Japan's bid to explain itself takes it further out on a limb

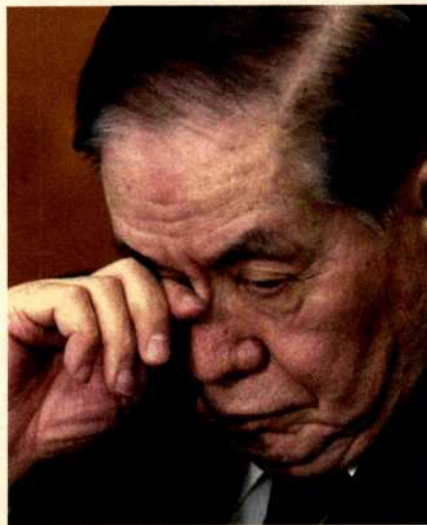
WHEN central bankers gamble, they usually go about it like pensioners in a low-stakes card game. "Should we lower interest rates, or stand pat? Let's try a quarter-point and hope for the best." But that, apparently, is not how it works in Tokyo, where the Bank of Japan has recently decided to go for broke. The central bank is not, as many have long been urging, placing its bet on an all-out monetary stimulus. Rather, as its officials made clear this week, the bank's preferred game of chance is politics. The stakes: all that remains of its credibility.

After its surprise announcement last week that it will begin buying equities from the portfolios of the country's ailing banks, the common reaction was that the Bank of Japan had caved in to political pressure by giving succour to banks and their over-protective regulators. Waves of condemnation followed, including, on September 20th, an unprecedented short-fall of bidders at the Ministry of Finance's auction of ten-year Japanese government bonds. In response to the criticism, officials at the central bank have begun privately pressing their case. Their explanation is even more stunning than their original decision.

By taking such an unorthodox step, says one senior official, the Bank of Japan hopes to act as a "catalyst" in order to "ignite full-fledged efforts among related parties to deal with the [banks' bad-loan] problem." Although he admitted that there

had been political pressure, "explicit and implicit", to buy the shares, the official maintains that this was not the reason for the new policy. The Bank of Japan is trying to take the game to the rest of Japan's government, goes his argument, not the other way round. It is an independent decision, he says, "based on our serious concern about the state of the financial system... We are not 100% sure that this approach will work. It's a big gamble."

Another senior official was similarly blunt, saying that the timing of the Bank's decision was tied directly to Japan's politi-



Hayami's catalytic conversion

Brazil

Race against time

SAO PAULO

The markets are nervous about October's presidential election

BRASIL'S *real* fell to an all-time low this week, dragging other Latin American currencies down with it, as Luiz Inacio Lula da Silva of the left-wing Workers' Party maintained a strong lead in the polls before the presidential election on October 6th. Mr da Silva is making great efforts to present himself as a centrist: he now pledges to honour Brazil's debts, not renege on them. The markets are unimpressed, fearing he may quickly lose control of the country's precarious finances.

In August a \$30 billion package of aid from the International Monetary Fund was intended to soothe Brazil's election jitters. Yet as Mr da Silva has extended his lead, the *real* has fallen further—September 24th's record low of 3.78 to the dollar means it has lost almost 40% of its value this year. After the IMF deal was announced, the risk premium on Brazil's bonds—their yield above American Treasury bonds—recovered from 2,294 basis points (22.9 percentage points) to 1,687. This week the risk premium jumped back above 2,100.

The government mostly pays interest on its bonds linked either to the exchange rate or to the high interest rates set by the central bank, so the debt has ballooned. In July, government debt hit an unprecedented 62% of GDP, up from 53% a year earlier. August's aid relief brought the ratio down a few points, but this week's fall of the *real* is likely to push it to a fresh record.

The government has tried to stabilise the debt by running ever greater primary surpluses on the budget (ie, before interest payments). And, at the insistence of the IMF, Mr da Silva and the other main candidates promised to maintain a budget surplus of at least 3.75% of GDP next year. Still, the further the currency sinks, and the higher are the rates that investors demand for rolling over the debt, the bigger is the surplus needed to stabilise the debt ratio. Recent studies conclude that unless market conditions improve soon, Brazil's debt burden may become unbearable.

The government has some cash in hand and should get \$6 billion of the IMF loan by the end of the year—the rest will come during 2003. Graham Stock, J.P. Morgan Chase's regional strategist, thinks that the government has enough cash to survive until about Christmas, even if the bond markets stop rolling over any expiring government debt. However, the government has heavy debt expiries early

next year, so if market turbulence continues the situation could get grave.

In other words, if he does win, either outright on October 6th or in a second round of voting three weeks later, Mr da Silva will have only a short time to establish his credibility. There is plenty he could do. First, he could announce credible inflation targets. His advisers hint at a slight loosening of next year's central target, currently 4%. But by how much? He could copy Tony Blair's bold move on coming to power in Britain in 1997, and grant the central bank independence. Mr da Silva's aides do not rule this out. Rapid action to push through other urgent reforms—for example, of the deficit-ridden state pension scheme—would also impress the markets.

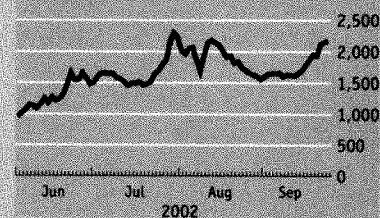
Mr Blair reassured investors by keeping on the governor of the Bank of England, Sir Edward George. Mr da Silva has dismayed markets by saying that Arminio Fraga, Brazil's trusted central-bank chief, must go. His advisers are less adamant, however, when asked if Mr Fraga might stay on a few months to help with the transition. This would be reassuring, as would be the appointment of a finance minister trusted by the financial markets—the Workers' Party has no such figure and would have to seek an outsider.

In his 1997 campaign, Mr Blair repeatedly promised to stick to the then Conservative government's spending plans for the coming two years. Mr da Silva, likewise, could keep reiterating a recent pledge to maintain a sufficient primary surplus to stabilise the government-debt ratio. Mr Blair swept to power with a crushing parliamentary majority (including many "New Labour" moderates), whereas Mr da Silva would have to seek a coalition, preferably a centrist one including some parties currently in the governing block. This would reassure markets that the unreformed lefties on the benches of the Workers' Party will not hold him to ransom.

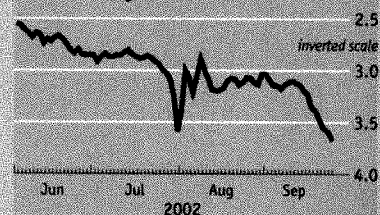
Brazil's banks are much stronger than Argentina's were before that country's default in December 2001 and its resulting banking collapse. Argentina's problem was that bank deposits and loans were largely dollarised, creating huge problems when its currency sank. That is not the case in Brazil. Nevertheless, says Victoria Miles, bank analyst at J.P. Morgan Chase, Brazilian banks have about 30% of their total assets (or 300% of their net worth) in government bonds. A forced restructuring

The Lula effect

Brazilian bond spreads over US Treasuries
basis points



Brazilian *real* against the dollar



Sources: J.P. Morgan Chase; Thomson Datastream

of Brazil's debt is still avoidable, she believes. But if it happened, the banking sector would face a "high level of stress".

In other words, Mr da Silva must realise how enormous would be the economic and political price of letting Brazil slide into default. To save the financial system in the event of a default, some sort of Argentine-style deposit freeze might be needed. Brazilians would never forgive him for that. If Mr da Silva wants to be sure of avoiding such a fate, he must act fast and he must act convincingly. ■

Investment banking in America

Unburdening

NEW YORK

Success on Wall Street has come to mean cutting people and problems

NO INVESTMENT bank has actually gone bust of late, and even disappointing results for the third quarter, announced over the past two weeks, show that most of the big firms nevertheless have returns on equity in double digits, or very nearly. Solace, presumably, to those still at their desk as colleagues are turned out on the street.

Still, panicky investors have pushed the shares of every major bank to their lowest level in years as they have watched falling stockmarkets, the thinnest of pickings for both mergers and acquisitions and the underwriting of new shares, and now the growing mass of litigation surrounding investment banks. Even the shares of Goldman Sachs, which likes to think of itself as being in a class above the rest, have dropped below the price on the day of ►►



Old days, empty streets

► Goldman's initial public offering in 1999.

Over the past year, costs at the eight biggest Wall Street firms have fallen by one-fifth, or \$4.3 billion. In New York, 20,000 jobs in the securities industry have been lost, a tenth of the total. The same number again will need to go in order to match post-bubble reality, says Svilen Ivanov of the Boston Consulting Group. Even the few investment banks that are not cutting their numbers, such as UBS Warburg, are nevertheless getting rid of dull performers, to replace them with those they expect to be more stellar. Meanwhile, out go fancy dinners and even, heavens, business-class flights.

If there was a surprise in the latest batch of results, it was the sharp jump in earnings posted by Goldman, which managed to increase profits by 12%. Yet because the source of these earnings is buried deep within the bank's proprietary-trading operations, the numbers have been viewed more with bewilderment than admiration. The top prize for performance goes to Bear Stearns, a grittier firm which managed to post quarterly earnings up 22% while revenues fell by 4%.

Bear Stearns's recipe? A strong market for mortgages, a speciality, helped. So did higher earnings from brokerage operations that cater to hedge funds, another house strength. Such funds have held big short positions as stockmarkets have slumped. Bear Stearns earns money from lending the funds shares to sell.

The firm also benefited simply because it never was a force in mergers and acquisitions or offerings, to which so many others committed huge resources. Yet perhaps the biggest reason for Bear Stearns's success is that it began a determined cost-cutting drive a year ago, when many firms held out hope of a quick recovery. Others

Credit Suisse

Twin peaks

Are two new bosses better than one?

LUKAS MÜHLEMANN may have been deposed only last week as head of Credit Suisse, Switzerland's second-biggest financial group. Yet he had been weakened at least since last year, when he forced out a Credit Suisse veteran, Oswald Grübel, head of private banking, and replaced him with Thomas Wel-lauer, a pal from his days at McKinsey. Mr Mühlemann then fired his protégé and called back Mr Grübel when he needed a scapegoat for the group's troubles. The only surprise is that news of Mr Mühlemann's departure did not come sooner.

Mr Mühlemann leaves an unenviable legacy. Five years ago, as an enthusiastic believer in *Allfinanz*, the notion of providing a one-stop shop for insurance and banking services, he bought Winterthur, Switzerland's biggest non-life insurer. Winterthur's capital strength certainly helped the group in the wake of Russia's financial crisis in 1998. But in June this year Sfr 1.7 billion (\$1.1 billion) had to be pumped into a much weakened Winterthur. Mr Mühlemann also led the takeover of Donaldson Lufkin & Jenrette (DLJ), an American securities firm, in 2000—the start of a vicious bear market. More than half of DLJ's staff have since gone. The entire investment-banking arm, CSFB, is surely worth less than the \$12 billion paid for DLJ alone.

The new management structure is less than perfect. Walter Kielholz, the chief executive of Swiss Re, a reinsurer, is the new chairman; he never wanted the job. The role of chief executive is to be shared by John Mack, head of CSFB, and Mr Grübel, who runs Credit Suisse Financial Services, which includes Winterthur. Mr Mack backed Mr Mühle-

mann when he sacked Mr Grübel.

A takeover of Credit Suisse, even in part, might be desirable, yet it is unlikely. What foreigner would want to buy Winterthur with its financial black hole? Competition authorities would probably block rival Swiss insurers. As for CSFB, Deutsche Bank, for one, needs to beef up its investment banking, but it denies any interest. No wonder: its shares would plummet. Bank of America appears to have ruled out buying CSFB, given that firm's troubles with American regulators. If Rainer Gut, still a power in the background at Credit Suisse, has his way, the group will never sell the investment bank that he pushed into the top league on Wall Street.

Despite the potential for power struggles, Mr Kielholz insists that the management overhaul is not a temporary arrangement. He is expected to give up his job at Swiss Re at the end of the year in order to take on the Credit Suisse chairmanship full-time. Meanwhile, the intention is to give more autonomy to the group's investment-banking arm and to Winterthur.

Mr Mack and Mr Grübel have a gargantuan task in reviving the fortunes of their respective businesses. Since he took charge in July last year, Mr Mack has laid off 3,000-odd bankers and slashed costs by \$2 billion. He is now working through the bank's pile of bad debts. CSFB took on excessive credit risk in the hope of generating investment-banking revenues, says David Williams at Morgan Stanley. Mr Grübel will have to take care of an ailing insurer as well as all of the group's retail and private banking. Perhaps the two new top dogs will simply not have much time to fight.

have since got the message.

Most investment banks feel that even if they cut staff too far, they can always rehire if business picks up. Weighing more uncertainly is the fear of litigation. Citigroup, for instance, is being scrutinised by the Securities and Exchange Commission, New York's attorney-general, the Justice Department, Congress and Manhattan's district attorney—among others.

Last week, the National Association of Securities Dealers (NASD) announced that it was imposing a \$5m fine on Citigroup's Salomon Smith Barney subsidiary, for publicly hyping Winstar, a telecoms company, at the same time as it was privately urging others to sell. Winstar is now bank-

rupt. Were the settlement the end of Citigroup's problems, Winstar would not have been such a bad transaction. According to the NASD, Salomon Smith Barney received \$24m for underwriting \$5.6 billion-worth of Winstar securities. Investors might have lost buckets, but Citi still looks \$19m ahead after the fine.

As part of the announcement, however, the NASD helpfully mentioned other, "larger" investigations into the bank's vilified research—by itself and by other regulators. At what point does Citi's reputation begin to crumble? Even if the litigation can be settled, the attention of senior management has shifted from running the business to defending it. ■

Economics focus First will be last

Internet economics has proved a bit of a disappointment

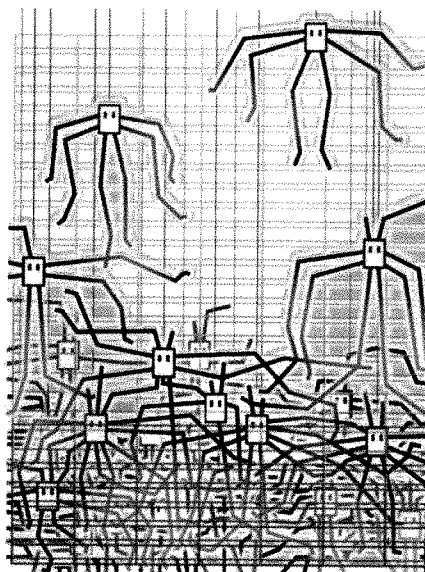
IN THE late 1990s, firms bet billions of dollars on a theory that turned out to be wrong. It said that in e-commerce, what mattered most was being first. Don't worry about being best, if that slows you down. Sell your product at a loss, give it away, pay people to take it: just build your base of customers fast. Why? Because the weird economics of the Internet—network effects, enhanced economies of scale and lock-in—gave a decisive advantage to first-movers.

Now that something approaching 100% of the Internet economy's first-movers have gone bust, this theory looks less plausible. Yet the logic once seemed persuasive. Where exactly did Internet economics go wrong? A new book by Stan Liebowitz, a professor of economics at the University of Texas at Dallas, and a long-time sceptic of the view that the Internet changes all the rules, gives the most thorough answer so far. "Re-Thinking the Network Economy"^{*} explains what the Internet did change and what it did not, so far as economics is concerned—and it does so in a witty and accessible way. It is the best book to date on the fallacies of the e-commerce craze.

Mr Liebowitz covers a lot of issues: the exaggerated advantages of Internet retailing over conventional retailing; the false claim that the Internet's lower costs would give Internet firms bigger profits; the inadequacies of the broadcast-television model of advertising revenues; the poorly understood questions of copyright and digital-rights management. But the crux of the book is two chapters devoted to attacking the theory of lock-in. This was the notion that caused the biggest mistakes—and the area where many economists were most at fault.

They just didn't get it

As the story was told, Internet lock-in happens largely because of network effects. When the value of a product to consumers increases with the popularity of the product, that is a network effect. (A telephone is worthless if you own the only one; the wider the network, the more useful a phone becomes.) Given strong network effects, a company that gains a big share of the market will be protected from competition from late-movers. Even a plainly better product may fail, because people, much as they may prefer it in itself, will wait for others to buy it first. The implication for busi-



ness is that moving first is all-important.

In refuting this, Mr Liebowitz emphasises the distinction between two kinds of lock-in. The question of compatibility is central to both. One kind of lock-in arises simply because switching to a new product involves a cost beyond the purchase price: costs of learning how to use it, for instance, or the difficulty of using it alongside products you already own. Mr Liebowitz calls this self-incompatibility, or weak lock-in. But there is also strong lock-in. This arises if a new product is incompatible with the choices of other consumers—and if, because of network effects, this external incompatibility reduces the value of the product.

The point is that weak lock-in is very common, indeed pervasive. Many new products have to overcome self-incompatibility. People do not buy a new computer every three months even though the product is improving all the time. Learning to use a new word processor is a bore; for most users, a rival has to be much better, not merely a bit better, to be worth the trouble. Note that if slightly better products are rejected because of self-incompatibility, this is not inefficient: it would be inefficient to buy such a product, incurring all the costs, unless the improvement was big enough to justify it. To repeat, weak lock-in is nothing new.

Strong lock-in is different, because of the network aspect. Strong lock-in means that consumers won't move to a new and much better product unless a lot of others

jump first. If they could somehow agree to move together, they would all be better off. But they cannot. Strong lock-in reflects a failure of co-ordination, it causes economic losses, and in theory it does create opportunities for decisive first-mover advantage. But how common is it, even in the new economy? Mr Liebowitz is forthright on this. Strong lock-in is not merely uncommon, he says, there is actually no known instance.

The lock-in literature leans heavily on just two examples: the persistence of the supposedly inferior QWERTY keyboard (see our Economics focus of April 3rd 1999) and the triumph of the VHS video standard over the supposedly superior Betamax. Both examples, Mr Liebowitz shows, turn out to be bogus. The QWERTY keyboard is about as fast to use as the most plausible alternatives, and VHS had important non-network advantages over Betamax—notably, longer tapes. Neither case shows strong lock-in.

Name a plainly superior technology that society has set aside not because of private cost or self-incompatibility, but because wide adoption was a precondition for its success. Not easy. Network effects do exist, and in principle they could work as the advocates of strong lock-in say, but in practice they have turned out to be far milder than e-commerce zealots supposed—in case after case, too weak to suppress plainly superior products.

Long before the Internet, consumers had plenty of experience adopting better technologies despite network-effect obstacles: cars (you need petrol stations), telephones, fax machines and, most recently, generation upon rapidly succeeding generation of network-dependent consumer-electronics devices. If a new product offers a clear margin of improvement over a competing one, consumers not only want to take it up themselves, they expect others to do the same. In this way, even where network effects apply, a sufficient margin of improvement achieves the necessary co-ordination among consumers.

In short, quality matters. Even in industries where the winner takes all (also rarer than you might think), having the best product matters more than being first to market. That may be old economics, but keeping it in mind would have saved a lot of people a lot of money. ■

^{*}Published by AMACOM, \$27.95

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Scientific fraud

Outside the Bell curve

A major scientific fraud has just been confirmed

THE sound of swallowed pride is rare but welcome. Bell Laboratories, one of the most venerable names in science, the home of the transistor and currently the research arm of Lucent Technologies, is prouder than many. But it has been taken for an enormous ride, and on September 25th it had the grace to admit it.

That was the day that a report into the activities of Jan Hendrik Schön, one of the laboratory's highest-flying physicists, was released. Dr Schön has spent the past few years turning out results of a quantity and apparent quality that were, until a few months ago, universally acknowledged to be worthy of a Nobel prize. Unfortunately, he seems to have made them up.

Moreover, he did so in a surprisingly artless way. Though suspicions were aroused when other labs could not duplicate them, these suspicions were generally explained as the result of differences in equipment. Indeed, the fact that Dr Schön could, by his own admission, achieve some findings only 10% of the time helped to allay people's fears. It began to look as if a quirk of his kit might be responsible, and the search turned to what that quirk might be. What caught him out in the end was

that he used identical (though differently labelled) graphs to illustrate papers in fields as diverse as the physics of semiconductors and superconductors.

When that emerged in May, Bell Labs immediately formed a committee of independent scientists, under the chairmanship of Malcolm Beasley, a respected physicist from Stanford University, to investigate what had happened. It is their report that has just been published.

What a tangled web we weave

Semiconductivity and superconductivity are critical to electronics. Dr Schön began his career looking at semiconductors made not of silicon (the preferred material for most commercial applications), but of organic molecules. In chemical parlance an organic molecule need not necessarily have come from a living creature. The term refers to molecules (often quite complex ones) that are built around a skeleton of interlinked carbon atoms.

Materials made of organic molecules are often flexible (plastics are organics). They are often cheap to manufacture too. But although signs of semiconductivity had been observed in a group of organic

molecules called pentacenes, no one had been able to use them to build actual semiconducting devices, such as transistors.

So when Dr Schön announced, in 2000, that he was able to make transistors out of pentacene, and then went on to demonstrate a number of abstruse semiconducting phenomena, such as the quantum Hall effect, in his pentacenes, everybody sat up and took notice.

He then capped this work by taking buckminsterfullerene, another organic molecule (also known as a buckyball because it has the shape of a miniature soccer ball), and, so he claimed, turning it into a superconductor. Not any old superconductor either. His bucky-superconductors worked at surprisingly high temperatures.

Superconductors (so called because they conduct electricity without resistance) work only below a certain, critical temperature. For the original superconductors, discovered almost a century ago, that temperature was so close to absolute zero that commercialisation was very restricted. In the late 1980s, it was found that some materials called perovskites would superconduct at temperatures higher than 77° above absolute zero. That meant they could be cooled with liquid nitrogen, which is cheap. Perovskites, however, are difficult to fabricate, so commercial applications were still limited.

Dr Schön's first bucky-superconductor "worked" at 11° above absolute zero. Through a carefully staged set of "improvements" to the technique, he got this up to 117°—well into the liquid nitrogen zone. Buckyballs are a discovery looking for an

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► application, and it seemed as though Dr Schön alone had found one.

And that last sentence holds the key to the fraud. For modern science is generally a collaborative effort. All of Dr Schön's 90 papers had co-authors—people who should, if things had worked the way they are supposed to, have been able to vouch for the quality of the research. But in practice, Dr Schön was actually working by himself. As the Beasley inquiry report puts it: "None of the most significant physical results was witnessed by any co-author or other colleague." That did not stop them putting their names to the work, though.

It did not stop the report exonerating all the co-authors either: "The committee does not endorse the view that each co-author is responsible for the entirety of a collaborative endeavour." In other words, where more than one person might carry the can, nobody shall be to blame. Except, of course, Dr Schön. But he is no scapegoat. The fraud was his responsibility. So are the millions of dollars that have been wasted following his "results" up. He will never work in science again.

20:20 hindsight

Mistakes happen. The important thing is to learn from them. There are probably two lessons to learn from this sordid episode. The first, in case anybody had forgotten, is that scientists are humans too. Some of them will do stupid and mendacious things. The second, and more important lesson, is that you can't cheat nature.

There will probably be a lot of finger-pointing at the system of peer review, in which journals send papers out to independent experts to be evaluated. Some scrutiny of the peer-review process might be welcome. In this case the results were so exciting that critical faculties may, on occasion, have been suspended. Indeed, several people have commented in retrospect that the results were too good. They matched theory exactly, which is unlikely both because experiments and theory are rarely in perfect agreement—particularly with preliminary work—and because the theories were developed for inorganic semiconductors such as silicon. It really would be a surprise if organic semiconductors were to behave in exactly the same way as inorganic ones.

The harshest examiner, however, is not a scientist's peers, but reality itself. The more significant a result is, the more it will be tested by that reality. In the case of Dr Schön's results, several of which had technologists licking their lips in anticipation of the inventions that might flow from them, the reality test was going to be enormous. How he expected to get away with it is mysterious. So, perhaps there is a third lesson as well. If you do cheat at science, do so in a field which is so insignificant that no one will bother to check. ■

Diesel engines

Hybrid vigour

A small electric motor can boost the performance of a diesel

BETWEEN the fuel cells that will power the cars of the future and today's petrol and diesel engines lie hybrid internal-combustion/electric vehicles. No one now believes that battery-driven electric cars will take over: the batteries are too heavy and run down too quickly. But cars that get their electricity from an internal-combustion engine acting as a generator are a reality. Two such hybrid vehicles, the Toyota Prius and the Honda Insight, are already selling in America and Japan. However, they cost about \$3,500 more than normal models, and weigh more than conventionally powered cars.

The trouble is that having two propulsion systems doubles the engine weight. In addition, there is a need for extra equipment to control the way that the two systems interact, and such control electronics are notoriously heavy. Ricardo, an engine consultancy based in southern England, has just unveiled a hybrid car which addresses these problems. Working with Valeo, a leading French car-parts maker, it has started with a conventional two-litre diesel-powered Opel Astra and converted it to hybrid propulsion.

The Astra produced 100 horsepower, but Ricardo was able to get the same output by fitting a lighter 1.2 litre turbo-diesel, that had state-of-the-art technology such as "common-rail" fuel injection, variable valve geometry and a turbo-charger. That improved efficiency. But there was one disadvantage—a lack of torque (pulling power) at low engine revs. Which is where the electric drive comes in. In an arrangement that it calls "mild hybridisation", Ricardo has rigged up an electric motor that

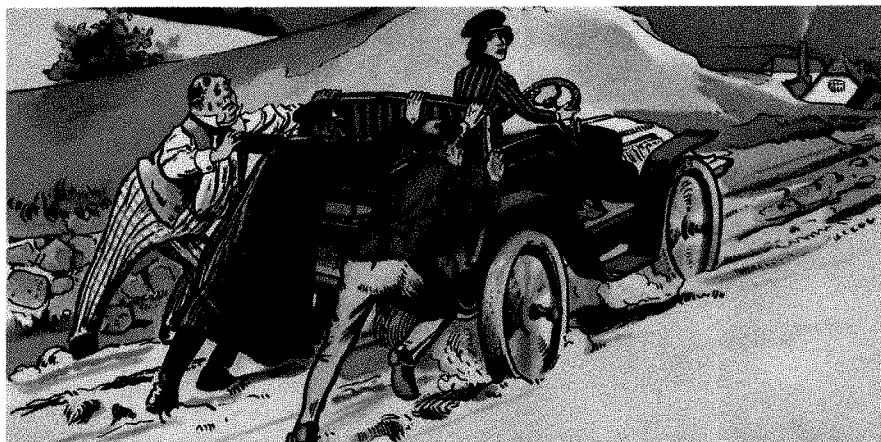
delivers extra power (6kw at 42 volts) if the engine is turning over at less than 2,000 revolutions per minute. This allows the car to accelerate as rapidly as the original, but its fuel consumption is 20% less.

The Ricardo/Valeo prototype uses a number of tricks to reduce weight. The principal one is that the diesel engine's fly-wheel is wrapped with wiring, allowing it to double up as the core of the electric motor. In addition, the choice of a 42-volt output means that all the car's requirements for ancillary power—for the cooling fan, air conditioning, lights and so on—can be provided by this generator. There is therefore no need for the diesel to have its own alternator-driven electrical system, a significant weight saving.

Fuel consumption is a thrifty four litres per 100km (70 miles per gallon) and emissions of carbon dioxide (CO₂) are claimed to be between 30% and 35% lower than the pure diesel version—a useful consideration given that European car producers are committed to a 25% reduction in CO₂ emissions across their car fleets by 2004.

Indeed, Europe is seen as the main market for the Ricardo/Valeo concept. The demonstration vehicle has been shown to the bosses of all the leading car companies. For them, the principal attraction of such a system is that the mild hybrid should cost only about \$1,000 more to make than a conventional vehicle.

The motor industry more or less agrees that hybrids are the next big thing. The only question is how to get the best out of them without adding too much weight or complexity. The Ricardo/Valeo idea of a miniaturised diesel engine is an ingenious step forward. Even in America, where nobody cares much about CO₂ emissions, hybrids are viewed as a way of reducing the huge thirst of big sport utility vehicles. The idea being considered by manufacturers there is to have an electric motor driving two wheels and a petrol engine driving the other two. If the systems can be made to work in harmony, there could be great savings just down the road. ■



They should have bought a hybrid

Strokes and heart attacks

An inside job

Some new ways of preventing dangerous blood clots

CURRENT estimates suggest that half of the people living in North America and Europe will die from a blood clot in a vital organ such as the heart, the brain or a lung. Preventing clots is therefore an important goal, and two recent advances have brought that goal nearer.

Athan Kuliopulos, of the New England Medical Centre in Boston, and his colleagues have focused on cellular receptors. Body cells bristle with receptor molecules that react to chemical messages from elsewhere. If these receptors are blocked, the cell does not know what is happening in the outside world, and so does not react.

Many drugs work by blocking receptors. In particular, more than 50% of prescription drugs stick to a group of molecules known as G-protein-coupled receptors (GPCRs). There are more than 1,000 types of human GPCR. Two of them are responsible for deciding when platelets—the cellular fragments that create blood clots—should stick together to form such a clot. Blocking these two receptors should prevent clotting. Doing so, though, has proved an intractable problem.

Dr Kuliopulos decided that if he could not block them on the outside of the cell's external membrane (the traditional way of doing these things), he would, as it were, go through the back door and block them on the inside of the membrane. The trick was to get the blocking agent—a fragment of protein known as a peptide—across that membrane. He achieved this by attaching the peptide to a molecule made of the same stuff as cell membranes. The result was a combined molecule, called a pepducin, that partially dissolves in cell membranes, and thus can penetrate them.

The new agent will have to go through many years of testing before it can hope to become a drug. But Dr Kuliopulos says that experiments in mice and on human blood cells—described in this month's *Nature Medicine*—have shown that his pepducin blocks both of the relevant platelet GPCRs. It therefore has the hallmarks of a powerful anti-clotting agent.

Although there are many existing anticoagulants, none is perfect. Pepducins may be able to help the 5-7% of patients who react adversely, or not at all, to existing ones. Blocking the receptors on the inside of the cell in this way also turns out to be a completely novel method of disabling GPCRs. So the researchers think that pepducins have potential as drugs affecting

Internet connectivity

Making the Web world-wide

A project in Laos is giving Internet access to villagers without electricity

“THE creation of the PC is the best thing that ever happened,” said Bill Gates at a conference on “digital dividends” in 2000. He even wondered if it might be possible to make computers for the poor in countries without an electric power grid. The answer is yes, and things are going even further. Villagers in a remote region of Laos that has neither electricity nor telephone connections are being wired up to the Internet.

Lee Thorn, the head of the Jhai Foundation, an American-Lao organisation, has been working for nearly five years in the Hin Heup district. The foundation has helped villagers build schools, install wells and organise a weaving co-operative. But those villagers told Mr Thorn that what they needed most was access to the Internet. To have any hope of meeting that need, in an environment which is both physically harsh and far removed from technical support, Mr Thorn realised that a robust computer was the first requirement.

He therefore turned to engineers working with the Jhai Foundation, who devised a machine that has no moving, and few delicate, parts. Instead of a hard disk, the Jhai PC relies on flash-memory chips to store its data. Its screen is a liquid-crystal display, rather than an energy-guzzling glass cathode-ray tube—an exception to the rule that the components used are old-fashioned, and therefore cheap. (No Pentiums, for example, just a 486-type processor.) Mr Thorn estimates that, built in quantity, each Jhai PC would cost around \$400. Furthermore, because of its simplicity, a Jhai PC can be powered by a car battery charged with bicycle cranks—thus removing the need for a connection to the grid.

Wireless Internet cards connect each Jhai PC to a solar-powered hilltop relay station which then passes the signals on to a computer in town that is connected to both the Lao phone system (for local

other GPCRs, and thus other diseases.

Preventing platelets from clotting is just one means of preventing blockages from forming inside blood vessels. Another is to stop those vessels becoming inflamed, and thus being susceptible to such blockage in the first place. In an article in the current issue of *Stroke*, John Hallenbeck, of America's National Institute of Neurological Disorders and Stroke, and his colleagues showed that they could vaccinate against the sort of inflammation that con-



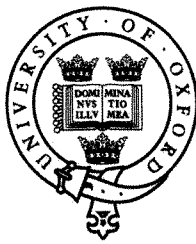
Modern technology, anybody?

calls) and to the Internet. Meanwhile, the Linux-based software that will run the computers is in the final stages of being “localised” into Lao by a group of expatriates in America.

One thing that the new network will allow villagers to do is decide whether it is worth going to market. Phon Hong, the local market town, is 30km away, so it is worth knowing the price of rice before you set off to sell some there. Links farther afield may allow decisions about growing crops for foreign markets to be taken more sensibly—and help with bargaining when these are sold. And there is also the pleasure of using Internet telephony to talk to relatives who have gone to the capital, Vientiane, or even abroad.

If it works, the Jhai PC and its associated network could be a widespread success. So far, the foundation has had expressions of interest from groups working in Peru, Chile and South Africa. The prototype should be operational in Laos this December and it, or something very much like it, may soon be bridging the digital divide elsewhere as well.

stricts blood vessels, thereby reducing the frequency and severity of strokes in experimental animals. They did this by interfering with a protein called E-selectin, which contributes to inflammation. By exposing rats to E-selectin, they were able to provoke an immune response to this protein. That meant that the rats produced antibodies against E-selectin when blood-vessel cells started to turn it out. The antibodies knocked out the protein and thus suppressed the inflammation. ■

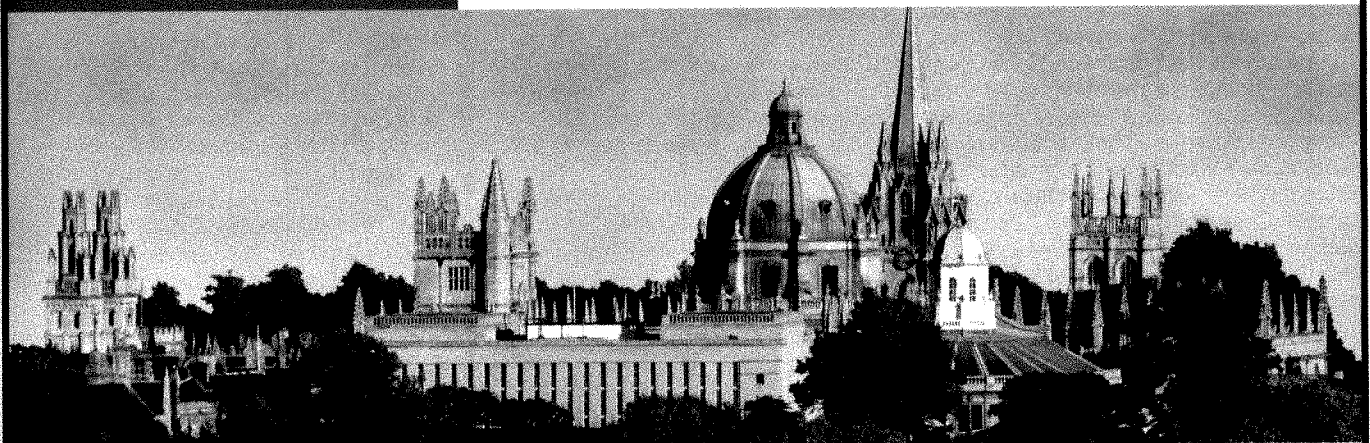


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American politics

Is America moving leftward?

If you think this sounds like a question from planet Pluto, then read this book

IN 1969, a young conservative activist named Kevin Phillips predicted the emergence of a Republican majority in the United States. It was a bold thing to forecast at the time. Richard Nixon had just won the White House by a narrow margin, only the second Republican to gain the presidency in 36 years.

Seen from today, Mr Phillips's prediction looks pretty good. Republicans have occupied the White House for 21 of the 33 years since he wrote. Had it not been for the Watergate scandal that drove Nixon from office and handed the Democrats victory in 1976 against the mood of the times, the Republicans' run would probably have been even longer.

Now, two years into the presidency of the narrowly elected but currently very popular George Bush, John Judis, a writer at the *New Republic*, and Ruy Teixeira, of the Century Foundation, offer an equally bold but opposite prediction. Working as Mr Phillips did from demographic trends and voting patterns, they foresee an emerging Democratic majority.

Their thesis is not entirely original. In 1996 a *Washington Post* columnist, E.J. Dionne Jr, predicted a Democratic and liberal revival in "They Only Look Dead". Mr Phillips himself in "Wealth and Democracy", pointed earlier this year to what he believes is an impending crisis for Republican conservatism. This book by Messrs Ju-

The Emerging Democratic Majority. By John B. Judis and Ruy Teixeira. Scribner; 224 pages; \$24

dis and Teixeira, however, is so crisply clear in its exposition and so skilfully supported by statistical evidence and analysis that it may finally turn conventional wisdom on its head.

Simply put, their thesis is that the conditions which led to the Republican era were over by 1992. Without working-class Reagan Democrats, without moderate suburban Republicans, and above all without California, it was impossible to sustain a durable conservative majority. Since then, the social foundations for a lasting Democratic majority have been properly laid.

That Republicans are still in charge, and may remain so after November, is due, they allow, to Bill Clinton's personal misconduct and to September 11th 2001. But the new majority, they insist, is ripening. They see the shift as bound up with changes that America has undergone in the past 30 years, "from an industrial to a post-industrial society, from a white Protestant to a multi-ethnic, religiously diverse society...and from a society of geographically distinct city, suburb and country to one of large, sweeping post-industrial metropolises."

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The authors move easily from electoral analysis through perceptive observation of sociological change to ambitious but plausible generalisations about the new Zeitgeist. They deal politely but robustly with much conventional wisdom. They disagree with the view of an influential centre-right pundit, Michael Barone, that demography, religion and economic trends all favour the Republicans. The big population increases are in places that support the Democrats, they argue. They claim that conservative advocates systematically overestimate how many Americans regularly attend church. And they believe that, whatever may have been true in the 1980s, a majority of Americans strongly oppose *laissez-faire* policies on pensions and on health care.

The authors do not spell out in a wholly conclusive manner the precise connections between post-industrial change and Democratic revival. Nor are they always careful to distinguish the party contrast, Democrat-Republican, from the ideological distinction, liberal-conservative. Although there are relatively few liberal Republicans, there are plenty of conservative Democrats. It is they, in recent times, who have tended to decide American elections, voting the party ticket when their candidate is dependably right-wing but happily bolting to Republicans when, as in 1972 and 1980, he looks too liberal.

Messrs Judis and Teixeira make no secret of where their sympathies lie, and the predictions in this comprehensive study are also hopes. Conservative readers in particular may jib at some of their more partisan judgments. Indeed, another plausible view is the Floridisation of American politics, the idea that it is now in an exact two-party balance. Nevertheless, all in all, the authors make a persuasive case that ►►

▶ something is happening in American politics, and that it is not good news for the Republican Party or for conservatism.

The competence and honesty of corporate chief executives, accountants and stockmarket analysts have been questioned in a way not seen since Richard Whitney, a one-time head of the New York Stock Exchange, defaulted in 1938. White working-class men are returning to old allegiances. Minorities, including most of the fast-growing Hispanic and Asian populations, a large and growing majority of women, and now professionals (even doctors!) are voting Democrat. Events, the authors admit, could still throw their prediction off. In international crises Americans rally to their president, whatever his party. Yet the trend, they insist, is leftward. ■

History of science

Time's arrow

Science: A History 1543-2001. By John Gribbin. Penguin/Allen Lane; 672 pages; £25

MODERN science began when people realised, during the 16th century, that the ancient Greeks had been wrong about almost everything. Trusting their own observations rather than old dogma, the first scientists invented a new way of investigating nature, resulting in a deluge of discoveries that changed the world.

John Gribbin, an astronomer and popular-science writer, begins his sweeping new history of science in 1543, with the publication of two crucial books that helped to kick-start this process. One, Copernicus's "De Revolutionibus Orbium Coelestium" (On the revolutions of the celestial spheres), advocated a heliocentric model of the universe that, with the help of Galileo Galilei, swiftly deposed the flawed physical theories of Aristotle and Ptolemy. The other, Vesalius's "De Humani Corporis Fabrica" (On the fabric of the human body), began the process of turning biology into a science by encouraging hands-on anatomical investigation rather than the hand-waving medical theories of Galen. From these twin starting-points, Mr Gribbin's book follows the history of science along the two resulting strands of enquiry into the physical and life sciences.

This is no mere retread of scientific history's well-worn paths, however. Drawing on the latest scholarship, Mr Gribbin manages to cast new light on old and familiar stories, demolishes innumerable myths, picks apart fact and fiction, and exposes the factual roots of some of science's well-

known tales. Though he ridiculed the Aristotelean claim that heavy objects fall faster than lighter ones, for example, Galileo never dropped weights of different sizes from Pisa's leaning tower to prove it; the weights were dropped by Aristoteleans hoping to prove Galileo wrong.

Descartes, Mr Gribbin explains, invented the geometric system that bears his name after watching a fly buzzing around a rectangular room. And Newton's uncharacteristically modest remark that his accomplishments were the result of "standing on the shoulders of giants" is intriguingly revealed as a withering side-swipe at his hunchbacked arch-rival, Robert Hooke, to whom Newton refused to acknowledge any debt. (Mr Gribbin's examination of the complex relationship between Newton, Hooke and Edmond Halley is particularly illuminating.)

There are less familiar faces, too, alongside the usual suspects. As well as his contribution to the rehabilitation of Hooke (whom Newton airbrushed out of scientific history), Mr Gribbin champions Thomas Digges as the inventor of the telescope and bestows the title of "the first scientist" on William Gilbert, whose experimental approach to the investigation of magnetism did much to inspire Galileo.

The two strands of the narrative converge when the connections between them (such as the implications of geology for the age of the earth and the origin of species) intensify. The explanations, particularly in the thorny field of quantum physics, are excellent, and the selection of subject matter skilfully winnows a vast field. Mr Gribbin's prose is confident, and his amusing asides include an explanation of the origins of soda water and the observation that the length of a French nobleman's title was, by and large, inversely proportional to his social standing. The triumphant bringing together of genetics and cosmology in the final chapter is cleverly handled and provides a satisfying, and only slightly contrived, conclusion.

Mr Gribbin's is an unashamedly old-fashioned approach to the history of science. He is generous with biographical information and firmly advocates the view that science progresses by incremental steps rather than revolutions or paradigm shifts. He has no time for trendy post-modern interpretations of science, or the suggestion that scientific theories are merely faddish "social constructions" with no basis in reality. Rubbish, says Mr Gribbin: scientific theories are rooted in truth, and new theories are not merely different from old ones, but are measurably better. "Science: A History" is a splendid book. The endorsement of the late Roy Porter, Britain's foremost practitioner of the history of science, who died earlier this year, underscores the magnitude of Mr Gribbin's achievement. ■

Business leaders

Why them?

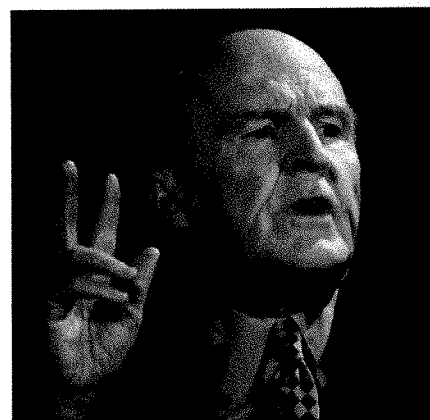
Geeks & Geezers: How Era, Values, and Defining Moments Shape Leaders. By Warren G. Bennis and Robert J. Thomas. Harvard Business School Press; 256 pages; \$26.95 and £19.99

OF ALL the reams on the stuff of leadership, some of the more sensible has been written by Warren Bennis. A California-based academic, adviser to American presidents and the bosses of some of the largest corporations in the world, he maintains that leaders are made not born. The gang leader in the playground does not end up running General Electric (or Iraq).

In his most famous book, "Leaders: Strategies for Taking Charge" (1997), Mr Bennis debunked the idea that leadership is relevant only to people at the top of an organisation, be it a nation, an army or a corporation. Anyone who can articulate a goal, then make others believe in it and pursue it, is a leader. The goal can be an outing to Disneyland just as it can be regime change in a distant country.

Now Mr Bennis and Robert Thomas, of Accenture's Institute for Strategic Change, have co-written this slight volume in which they argue that leaders are forged by the way they react to formative moments in their lives (which they call "crucibles"). The book is an extended report on a series of 43 interviews with subjects whom the authors have chosen for their leadership skills. All the subjects are American, many of them widely unknown. Just over half of them are "geezers" (people over 70 years of age), and the rest are "geeks" (under 35).

The authors have been unable to resist listing the four essential qualities that their research shows these people have brought to their crucibles, and that have made them (we must believe) great leaders. Of the four, the greatest apparently is "adap- ▶▶



Shakespeare, George Washington and me

► tive capacity", something shared by Shakespeare, George Washington and Jack Welch. In the end, it transpires, the four are nothing more than "the same factors that make a person a healthy, fully integrated human being". Possessed, it is tempting to ask, by people like Napoleon, Winston Churchill and Genghis Khan?

In the context of the current crisis of corporate leadership in America and Europe, the book has disappointingly little to offer. The "adaptive" leaders of Europe's media and telecoms giants are being bundled out in favour of old-school conservatives; while America is tussling with the discovery that, when the goal is the promise of great wealth, followers galore can be corralled and led by almost any semi-numerate adaptive thief. Anyone looking for insight into the behaviour of Kenneth Lay, Bernie Ebbers or Jean-Marie Messier should stick to Niccolo Machiavelli. ■

Civil war in Sudan

African queen

Emma's War: An Aid Worker, a Warlord, Radical Islam, and the Politics of Oil—A True Story of Love and Death in Sudan. By Deborah Scroggins. Pantheon; 389 pages; \$25. To be published in Britain by HarperCollins in March 2003

EMMA McCUNE was an idealistic young British aid worker who spent much of the late 1980s criss-crossing southern Sudan, then as now in the grip of civil war, dressed in a red mini-skirt. Handing out charity pencils, books and blackboards to outdoor schools financed by a high-minded Canadian lawyer, she cut a striking figure.

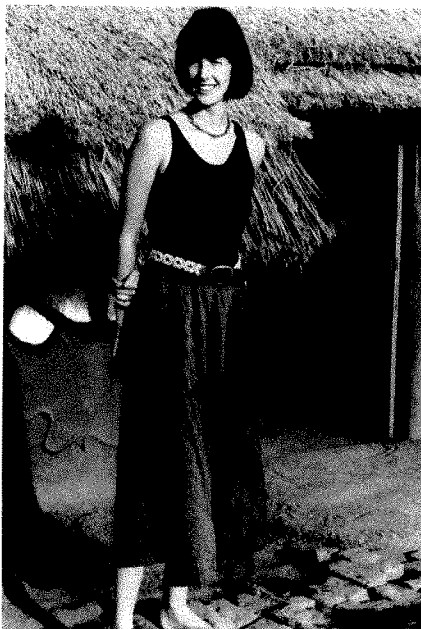
What really made McCune's name, though, was her marriage in 1991 to a southern Sudanese warlord, Riek Machar. McCune saw the marriage as a way of breaching the gap between white and black. But to her fellow aid workers, it seemed that she had crossed an invisible, and not altogether happy, line. When the Khartoum government began bombing Sudanese refugees who were fleeing back into the country from Ethiopia, the peaceable aid worker threw herself into Mr Machar's violent quest to take over southern Sudan's rebel movement. In thrall to the man, she paid little attention to the murder and kidnapping that was part of his quest for power. Two years later, McCune was dead, crushed by an itinerant bush taxi near Nairobi. She was 29 and pregnant.

Deborah Scroggins uses the romantic aspects of this beautiful white woman's story to draw in unsuspecting readers. But

she has a sharp eye, and her real aim is to tease out the inconsistencies of Emma McCune's brutally short life as a way of looking at how foreigners through the ages have involved themselves in Sudan.

The humanitarians of the 19th century, many of whom were driven by urges half-hidden even from themselves, have given way to modern famine-relief programmes. The donors who fund them like the idea of giving pencils to small black children. However, they averted their eyes when the hand-made sweaters donated by American knitting circles in the late 1980s proved too warm for the Sudanese (they ended up being worn as decorative hats) and when American food aid was used by the southern Sudanese rebel movement, the SPLA, to maintain scores of camps where kidnapped children were trained to fire guns. They looked away too whenever the Khartoum government felt that foreign aid was making southern leaders like Riek Machar too powerful, and retaliated by bombing feeding stations full of women and their stick-thin children.

American oil companies pay the northern Islamic government to try and gain access to the untapped oilfields that lie in the south of the country. So far, the violence has stopped Chevron and others from getting very far. At the same time, Christian groups in America pour money into financing the southerners against the Muslim north. They believe they are helping to establish a vanguard against the spread of Islam, but what they are really doing is fuelling the civil war. "Emma's War" is about the politics of the belly, and what happens when the fat white paunch meets the swollen stomachs of the hungry in Africa. It is a sorry story, but Ms Scroggins tells it awfully well. ■



On the road to hell

New American fiction

Pony express

The Fruit of Stone. By Mark Spragg. Riverhead Books; 304 pages; \$24.95. Jonathan Cape; £12

ADULTERY, mid-life crisis, cattle auctions and the spirit world: Mark Spragg's curiously titled first novel is no ordinary western. Two middle-aged Wyoming buddies, McEban and Bennett, are in love with the same woman, Gretchen, a comely redhead with a satchel full of 17th-century religious verse. Gretchen is married to Bennett, but, as the novel opens, has just leapt into bed with McEban.

McEban is a battered, lugubrious rancher, Bennett a real-estate salesman with a foul temper and a thirst for the demon drink. So it comes as no great surprise when, in chapter three, Gretchen decides to pack her bags and light out for the territories, abandoning both Bennett and McEban for a physicist from Colorado. "When you read this, I'll be gone," says the note Bennett finds on the kitchen table. "There's another man, but he's only part of the reason. He's the opportunity." Oddly, though, Gretchen invites Bennett to follow her, apparently in the belief that it will help him to understand why she left him. A further letter, she promises, will be waiting for him at the post office in Bozeman, Montana. Thus the two men set off on an unlikely paperchase across the prairie.

Mr Spragg's previous book, a memoir called "Where Rivers Change Direction", was well received when it appeared in 1999. Readers who liked the richly sensuous way he wrote about the Wyoming landscape in that book will find much to enjoy in "The Fruit of Stone". But here the fine writing is too hit-and-miss fully to compensate for the wacky storyline, and Mr Spragg lets himself down when he lapses into a sort of sub-Hemingwayesque tough-guy lyricism. A sentence like this one is typical in its slightly awkward combination of plain language and florid tone: "Halfway to the valley floor the sun gains the sky again and the Snake River glows as an uneven rend in the green country below them, and then they're in the little town of Wilson at the bottom of the pass and the smell of their burning brakepads fills the cab and it is fully dawn." Fully dawn, all right, and—whoa!—time to pull over, cowboy.

Elliott Carter

True notes

Elliott Carter's composing has never been more creative. And he's 93

THERE are Indian summers and there are Indian summers. There are composers whose creativity continues undimmed through their 70s and 80s; Giuseppe Verdi completed "Falstaff" at the age of 79, Igor Stravinsky was still seeking out new musical discoveries when he was 83. Yet how many are still working well into their 90s? Elliott Carter is one.

A venerated composer, Mr Carter is also one of the most venerable. Mark Twain was telling jokes to the *New York Times* the year Mr Carter was born in the city; in December he will turn 94. Through the decades, Mr Carter has created a musical language that uniquely fuses American iconoclasm and European historicism. Today, he is writing music of dazzling brilliance and subtlety; music that speaks with a playful, and even youthful, directness. His productivity has increased as he has struck out into new fields and forms, pouring forth a stream of pieces from intimate solo works to some of his most ambitious and imposing orchestral scores.

Mr Carter completed his largest-ever orchestral work, a huge triptych, "Symphonia: Sum Fluxae Pretium Spei", at 88. He wrote his first opera when he was 90. Called "What Next?" and set to words by a British writer and critic, Paul Griffiths, this work about the aftermath of a car crash was premiered by the Berliner Staatsoper in 1999 under Daniel Barenboim.

Undaunted by his advancing years, Mr Carter also has a number of new large-scale commissions planned for the future. This year he is writing two new orchestral pieces, the Boston Concerto for the Boston Symphony Orchestra, and another work for the Chicago Symphony Orchestra. No world-weary swansong, this is an invigorating explosion of creativity.

Early fire

It was while he was still at school that Mr Carter's interest in modern music was fired up by his encounters with Charles Ives, the most radical of the early 20th-century American modernists. In the mid-1920s, the 50-year-old Ives took him to Carnegie Hall and recommended him to the dean of Harvard University. Later, Mr Carter travelled to Paris to refine his technique with Nadia Boulanger. He tried hard to assimilate the teaching of this legendary pedagogue and fountainhead of European neo-classicism into his musical aesthetic. But when he returned to America in 1936,

Mr Carter became aware that despite, or perhaps because of these daunting influences, he still had not found his true compositional voice.

The struggle that ensued would isolate him from composers like Aaron Copland and Roy Harris, whose artful simplicity appealed so directly to audiences in New-Deal America. Mr Carter's own voice did not crystallise until he was in his 40s, in the intensely dramatic Cello Sonata, completed in 1948, and even more startlingly in his First String Quartet of 1951. The quartet was composed during a year spent in the deserts of Arizona. This was not merely a physical separation from urban America, but an artistic one, too: a symbol of Mr Carter's rejection of his previous musical life, and the pervasive populism of post-war America.

The first quartet is a vast and unashamedly complex work, as rewarding as it is demanding for both players and listeners. Yet Mr Carter's music of the 1960s and 1970s surpasses even this piece in richness and range. Igor Stravinsky paid Mr Carter's 1961 Double Concerto an underhand compliment, hailing it as "a masterpiece, and by an American composer".

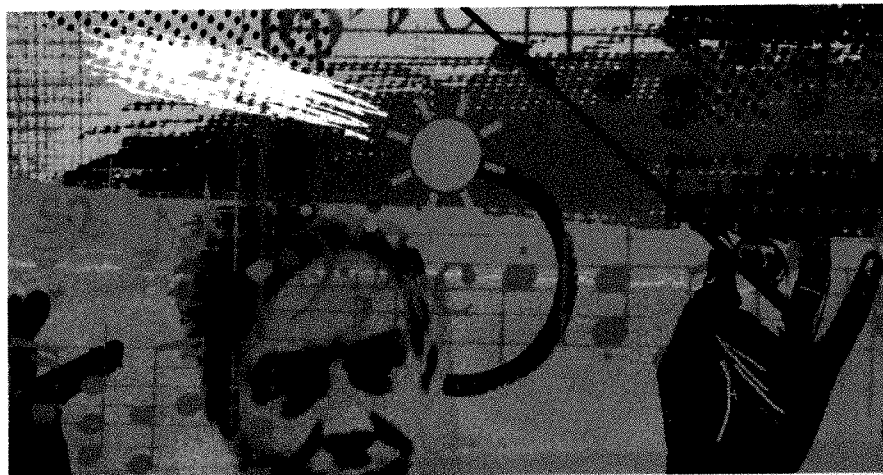
The Concerto for Orchestra, composed in 1969 for Leonard Bernstein and the New York Philharmonic Orchestra, is an essay in musical multivalence. The orchestra is divided into four groups, and their music progresses at different speeds simultaneously. The music is in a constant state of becoming, a metaphor for the ceaseless activity that Mr Carter observed in contemporary America. And the effect, of a whirlwind sonic tempest, turns the piece into a

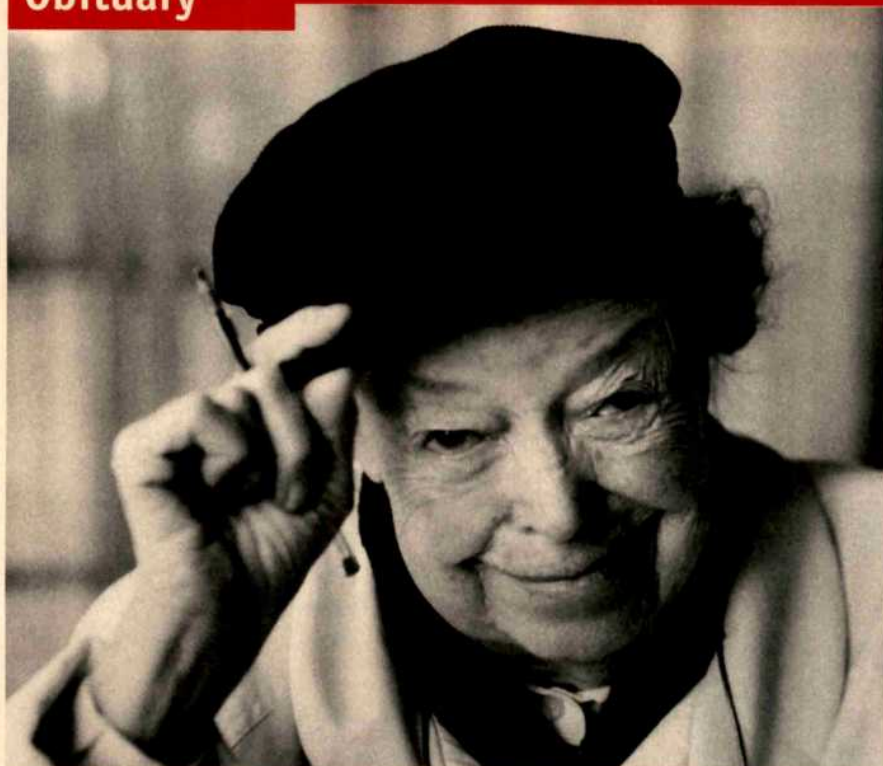
dazzling feat of poetic and technical virtuosity.

Over the past two decades, Mr Carter has refined this language. Many of the same concerns are there: an emphasis on tempo as well as harmony as a structural force, a laser-like ear for instrumental colour, and above all, the creation of a vivid depth of experience for performers and listeners. But there is an even wider expressive range in his recent works, which encompasses lightness and humour as well as power and seriousness. The Asko Concerto, composed in 2000 for the 16 players of the Dutch Asko Ensemble, is a contemporary concerto grosso, in which all of the players have their moment in the spotlight. Mr Carter has said that he wanted to create instrumental combinations that would be "fantastical and humorous", so the clarinet is paired with the double bass, the violin with the trumpet. The work closes with an outrageous bassoon solo, as free and jocular as anything in the repertoire.

Mr Carter is now able to mine the seam of musical material he discovered in earlier decades. He has created a language of uncompromising modernist integrity that embraces an intellectual spectrum from light-heartedness to profundity. It's a rich reward—for both the composer and his audiences—after the years of struggle. "Composition was at one time a matter of rejecting a lot of things I knew", he says, "and finally finding what I really liked most, and once I'd found that, it was easier to compose." It's a seam that shows no signs of being depleted.

Mr Carter hopes to enter a second century of composition with unlimited horizons, an achievement almost without parallel in the history of 20th and 21st-century art. The Latin subtitle of his *Symphonia* is taken from a 17th-century poem by Richard Crashaw, and translates as "I am the prize of flowing hope". It could stand as a motto for all the composer's recent music, every note of which is a prize won from 80 years of continuous creativity. ■





Joan Littlewood

Joan Maud Littlewood, a theatrical prodigy, died on September 20th, aged 87

MENTION Joan Littlewood and those that still remember her may murmur, "Oh! What a Lovely War" and perhaps hum a few notes of its theme tune. The play was first put on in 1963 and some 40 years later remains a powerful snub to the propaganda of war. It has had a worldwide audience. Not only was it seen in theatres in London, elsewhere in Europe and in the United States, but it was made into a film that reached the millions who never go to a theatre.

Its strength was that it was hugely entertaining, featuring the immensely tuneful songs of the first world war. But just as a nostalgic number was captivating its audience, a news flash would read, "Battle of the Somme ends. Casualties, 1,332,000. Gain, nil." The play spared no one, especially those in command. A British general prays, "Well, God, the prospects for a successful attack are now ideal... And I ask for victory, oh Lord, before the Americans arrive." The anti-war feeling of the 1960s that Miss Littlewood captured has endured, and the task of the war propagandist has never been harder.

"How I loathed those songs," Miss Littlewood said. They recalled a childhood of "photos of dead soldiers in silver frames, medals in a forgotten drawer". But she also loathed the commercial success of the

play, and of other plays she conceived and produced that went on to make heaps of money. Many ordinary mortals would be delighted that a production that started life in a tiny theatre had gone on to do well. But Miss Littlewood was not ordinary and to her admirers there was something a bit immortal about her as well.

It wasn't the money she objected to: for much of her life she was hard up, and many of the plays she produced were put on with little money. What she feared was that her work would be tainted by its connection with conventional theatre. She once said that Laurence Olivier was "the most stupid ham that ever conned people into taking him for an actor". She dismissed a young Michael Caine with her gravest insult: "You will only ever be a star." Noel Coward's "Private Lives" was the sort of play she couldn't stand. Understandably, many in conventional theatre didn't much care for her either.

Street theatre

At the start of her autobiography, "Joan's Book", Miss Littlewood describes a childhood of poverty in London and how at the age of six she was a bridesmaid when her mother finally married. But prodigies have a way of surviving unpromising beginnings. A church school and the local public

library provided her with the rudiments of education. At 16 she won a free place to Britain's leading acting school, the Royal Academy of Dramatic Art. In 1934, when she was 20, she joined a company called Theatre of Action, founded by Ewan MacColl, a folk singer she later married. It performed in the streets of Manchester and was one of several dozen such troupes in the north of England.

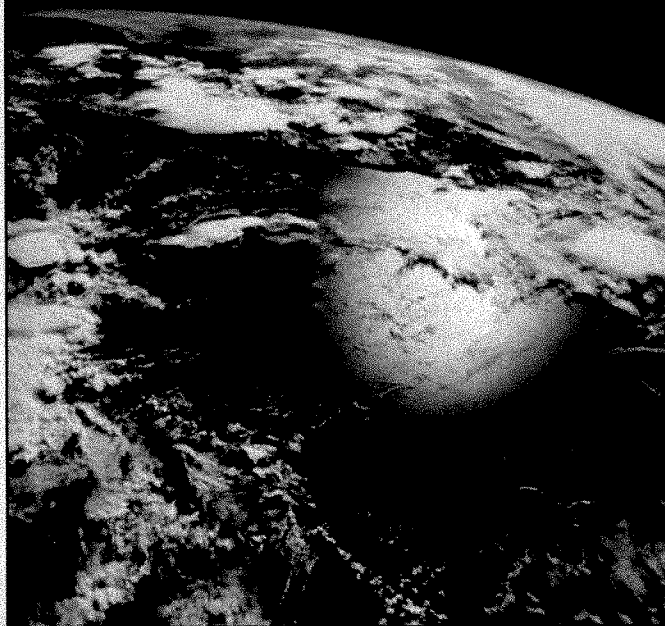
They modelled themselves on German theatrical troupes which were parodying the recently-installed Nazi government, and whose members would soon be rounded up and sent to concentration camps. Miss Littlewood's plans for a "people's theatre" stem from this time. Bertold Brecht, a German dramatist, was one of her heroes. In "Oh! What a Lovely War" there are echoes of Brecht's "The Threepenny Opera", of 1928, with its film clips and messages on cards. But revolution had to be put on hold during the second world war, when Miss Littlewood worked for the BBC, making a soap for transmission to American listeners called "Front Line Family". It was about "everyday people" and at the BBC "I was the only one who'd had contact with such glamorous creatures."

After the war, bursting with ideas and with a new husband, Gerry Raffles, nine years her junior, whom she had met when he was a teenager, Miss Littlewood once again set out to show ordinary people the magic of theatre. The trouble was, ordinary people were not much interested. "There was an audience for us somewhere, but where?" she said indignantly. In 1953 she and Raffles rented and later bought a once-graceful but now dilapidated theatre in Stratford, not on Avon but in rundown east London. Surely the locals would support the revival of one of their old playhouses, proudly called the Theatre Royal? They did not.

But her company did become famous abroad. It toured throughout Europe. Three plays the company did at a Paris festival in 1955 won rave reviews in French newspapers. The Stratford theatre was "discovered" by London critics and its seats were soon filled by middle-class people. They tolerated the classics, such as Ben Jonson's "Volpone", and loved musical productions such as "Fings Ain't Wot They Used T'Be". Several were transferred to theatres in central London.

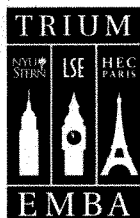
When Gerry Raffles died in 1974, Miss Littlewood gave up most of her theatre work. He had in many ways been her wife, taking on the domestic tasks she had no time for. For much of the rest of her life she lived in France, near Vienne, where he is buried. Joan Littlewood shook up British theatre, but only briefly. Seeing a play remains mostly a middle-class pleasure. "Private Lives" was recently revived with great success. ■

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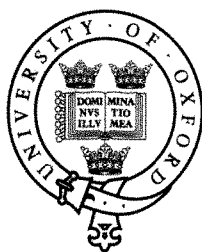
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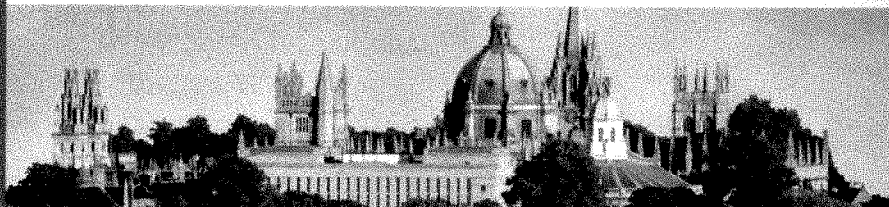
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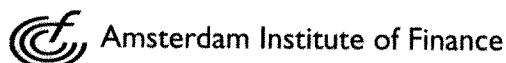
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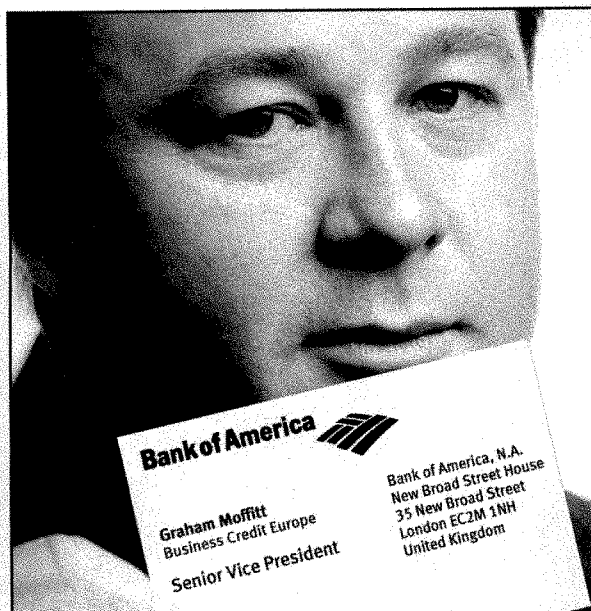
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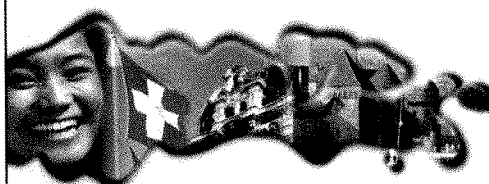
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The Malawi NSO is a central government body responsible for the production and dissemination of official statistics – and has a central role to play in the country's Poverty Reduction Strategy by providing quality statistical data to monitor and evaluate inputs, processes and results. The strategy will place a new set of demands on statistical systems – demands that will need greater coherence between the NSO and other producers and users statistics, if the figures needed for PRS monitoring are to be delivered effectively.

This, combined with a proposed move to semi-autonomy and relocation, means the NSO is entering a challenging new phase. You'll offer support to all these strategic processes – predominantly working to develop a system of national statistics that meet PRS monitoring needs. This will include governance arrangements, new legislation, agreeing a code of practice, and facilitating consultative processes. You'll also develop standards for collecting, processing and disseminating data, assess training needs, and build an overarching plan for the production of key outputs across the full statistical range. Moreover, we'll look to you for leadership on implementing the NSO's strategic plan and developing localised statistical capacity, as well as guiding the proposed relocation process.

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For more information on this vacancy, DFID in general, and an electronic application form, visit our website. Alternatively, call 01355 843129 or e-mail hrod4b1@dfid.gov.uk to request an application pack – quoting Ref. AH375/4LS.

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To support the growth of our work we have the following opportunity based in our UK secretariat in Brighton.

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Closing date: 11th October 2002. Interviews: w/c 29th October 2002

Qualified people living with HIV/AIDS are particularly encouraged to apply. For further information on how to apply, please e-mail recruitment@aidalliance.org. Please quote the reference number.

University of Qatar The National Center for Economic Research



Researchers

The National Center for Economic Research at the University of Qatar is seeking the appointment of qualified researchers to assist in implementing its program.

Potential candidates must hold a Ph.D degree (preferably from a Western University) in Economics/Finance or allied subjects, have at least two years of experience as academics/researchers and a number of publications in refereed international journals.

For enquires, please contact Professor Mohktar M. Metwally, Tel (+974) 4852823, fax (+974) 4832923, e-mail: metwally@qu.edu.qa

Applicants must e-mail a copy of their up-dated CV with names and e-mail addresses of two referees. Deadline for applications is 11 October 2002.



International Rescue Committee

www.theirc.org

Post Conflict Development Initiative Roster

The International Rescue Committee seeks experienced development professionals to work in countries undergoing the transition from relief to development. IRC recently established the **Post Conflict Development Initiative (PCDI)** to formalize IRC in the field of post conflict and relief to development transitions. IRC is gathering CVs of individuals interested in being included on a PCDI candidate roster. IRC seeks those interested in long and short-term opportunities, with expertise in the following areas: Civil society, cooperative development; Institutional strengthening and capacity building; local government; Training; Small business services; Agricultural market development; Food security; Reintegration, and rehabilitation; Conflict resolution; Property rights; Human rights and protection; Gender based violence; Grants program design and management; and Monitoring and evaluation. Candidates interested in being included on IRC's PCDI roster should send a resume and cover letter to: PCDIroster@theirc.org.

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The IRC seeks experienced candidates to serve as Chief of Party (COP) to manage large-scale transition and relief to development assignments of 3-5 years. **Requirements:** Prior COP experience, preferably for USAID projects; Masters degree in international development, economics, or related field; 5-10 years overseas exp. managing development assistance projects in developing countries; Experience in education, child survival, water and sanitation, health and/or income generation; Exp. managing USAID projects and knowledge of USAID policies and regulations; Expertise in gender, institutional strengthening, or NGO capacity development preferred. This position is contingent upon grant approval. Send a resume and cover letter by email to: PCDIroster@theirc.org.

INSTITUTIONAL STRENGTHENING EXPERT

The IRC seeks qualified candidates with experience strengthening the institutional capacity of NGOs, government institutions, and/or business entities, for short and long-term assignments. **Requirements:** 5-10 years overseas experience providing institutional strengthening services; Masters in organizational development, social science, international development, or related field; Experience in education, child survival, water and sanitation, health and/or income generation; Exp. conducting assessments using formal assessment tools, such as DOSA; Exp. developing and implementing strategic plans, sustainability plans, and monitoring and evaluation plans; Experience managing projects in difficult security environments. This position is contingent upon grant approval. Send a resume and cover letter by email to: PCDIroster@theirc.org.

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Attention: Dean, Graduate Business Programs,
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ULG NORTHUMBRIAN LTD

Fisheries in Bangladesh

The Fourth Fisheries Project in Bangladesh supports sustainable and equitable growth in the benefits generated from increased fish and shrimp production. The project provides support to fishing communities through the Department of Fisheries and national and local NGOs. DFID is funding the technical assistance and has contracted ULG Northumbrian, PMTC International and NR International to provide international specialists.

We are currently seeking candidates for the posts of Fisheries Management and Monitoring and Evaluation Specialists to start in late 2002 for 2 year contracts.

1. Fisheries Management

We are looking for a senior fisheries scientist with 10 years experience in the management and design of openwater fisheries (preferably inland) and with experience of the management of enhancements.

2. Monitoring and Evaluation

The candidate should have 10 years hands on experience as an M&E expert of which at least 5 years in developing and implementing information systems in private or government organisations or major projects.

Both posts require relevant post graduate qualifications and experience in Bangladesh or South Asia is also desirable.

More details can be obtained from Katie Collins. If you are interested, please send your CV by 14 October to Katie at ulg@ulg.co.uk quoting ref: **BDS4699 FM/ME**

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KINGDOM OF SAUDI ARABIA



SAUDI RAILWAYS ORGANIZATION

Advisory Services for Private Sector Participation in the Construction and Operation of a Railway Project

Request for Expression of Interest

Saudi Railways Organization (SRO) invites "Expression of Interest (EOI)" from world class Financial Institutions, to provide financial and technical advisory services to promote private sector participation in the construction and operation of a railway line from Riyadh to Jeddah (about 950 km) and from Dammam to Jubail (about 115 km). The financial advisers will also be required to explore the feasibility of including in the Project the proposed rail link (570 km) connecting Makkah to Jeddah, Madina and Yanbu.

Several studies on the proposed Project have been conducted by highly reputable organizations on behalf of the Government of Saudi Arabia. These will be made available to all the short-listed bidders.

The Advisers are expected to structure the Project to attract private sector financing on a BOT basis. They will be responsible for assisting SRO in the process of managing the "Request for Proposal" stage, evaluation of proposals and the formal contract arrangements. Towards this goal, they are expected to, among other things, review previous studies relating to the Project including the "Financial Model"; carry out a feasibility study of Makkah-Jeddah-Madina-Yanbu railway link; determine investment requirements; provide advice on the structure of private sector financing; prepare and implement a marketing plan; finalize route alignment, prepare land plans for the acquisition of privately owned land required for the Project; define performance and design parameters, draft the information memorandum and the request for proposals; participate, as required, in the evaluation of bids and negotiations with the potential investors and assist in the financial closure.

Expressions of Interest (EOI) from internationally reputed Institutions with the necessary experience of providing financial and technical services for comparable railway transactions should be submitted with the following details: (1) profile of the Firm/consortia including annual reports for the last 5 years; (2) a description of similar tasks carried out and role of the Firm and (3) reference clients contacts.

It is required that interested Financial Institutions will engage and provide the technical services of reputed Engineering Consulting Firms with solid railway experience to deal with technical issues not covered by earlier studies. Detailed qualification information of the Engineering Firm should also be submitted.

Detailed Terms of Reference will be supplied to the short-listed Advisers.

EOI should reach the following address (in both hard and soft copies) by 10-00 A.M. of Sunday, November 10, 2002:

The President

Saudi Railways Organization.

P.O. Box 36, Dammam 31241

Saudi Arabia.

Fax 00966-3-827-1130. Email: landbridge@sro.org.sa

New York University Fellowships Project on the Cold War as Global Conflict International Center for Advanced Studies

2003-2004 fellowships in the Project on the Cold War as Global Conflict at the International Center for Advanced Studies, NYU. For scholars with PhDs at all career stages in humanities and social sciences. Non-U.S. applications encouraged. \$35,000 stipend for 9 months. *Deadline:* January 15, 2003. Eligible for low-cost NYU housing.

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See <http://www.nyu.edu/gsas/dept/icas> for more information and application forms, or write to icas@nyu.edu, fax: 212-995-4546.

Tenders

GUATEMALA, CENTRAL AMERICA

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The Instituto Nacional de Electrificación -INDE- with the objective to promote the empowerment of the Central Thermal Power plant of Escuintla (CTE), Guatemala, invites through this announce to qualified consultants to participate in the presentations of offers to contract the Technical and Financial Advisor for this process. The requirements to participate are the following:

- Demonstrable technical capability for the analysis and determination of the best technical option for the Plant (CTE) empowerment.
- Demonstrable knowledge and capability to convoke development groups or private investors that have capability to lead to the sign of contract.
- Financial analysis capability to develop models and evaluation forms required by the project.
- comparable work experience in the conception, development and selection of developers, investors and implementation of generation processes up to 80MW.
- Demonstrable participation in electric generation projects during the last 5 years.

The cost of the terms of reference is US\$2500 or the equivalent in the national currency Quetzales, at the purchase exchange rate that publish the Guatemalan Bank for the day that the purchase will be realized. They will be available at the Gerencia de Servicios Corporativos Office located at Level N1 7a. Av. 2-29, zona 9, Edificio la Torre, Guatemala city, Central America, previous payment at the Treasurer Office, located at the same building.

**The offers in Spanish, must be delivered by the date limit
Wednesday October 16th, 2002 at 9.30 hours (Local time) at the
Board of Directors Saloon, located at the same building level
number one (7a. Av. 2-29 zona 9)**

Guatemala, September 2002

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The Trustees of the Houblon-Norman Fund invite applications for Research Fellowships tenable at the Bank of England during the academic year 2003/2004. The appointment will be for full-time research on an economic or financial topic of the candidate's choice, preferably one that could be studied with particular advantage at the Bank of England. The length of the appointment will be by agreement with successful applicants, but will not normally be less than one month, nor longer than one year. Senior Fellowships will be awarded to distinguished research workers who have established a reputation in their field. Fellowships will also be available for younger post-doctoral or equivalent applicants, and for these, preference will be shown to British and other EU Nationals. *The award will normally be related to academic salary scales.*

Application forms (to be returned
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Overview

Global **stockmarkets** fell again as fears of a war against Iraq, gloomy prospects for the global economy and shrinking corporate profits took their toll. America's Dow Jones Industrial Average fell to a four-year low. The Nasdaq fell to a six-year low. Britain's FTSE 100 fell by 2.4%, also to a six-year low. The yield on America's 10-year Treasury bond fell to 3.63%, the lowest level in 44 years, as investors sought shelter in bonds.

America's Federal Reserve kept interest rates unchanged, yet two members of its 12-member rate-setting board took the rare step of voicing their dissent in favour of lower rates.

American consumers remain anxious. The Conference Board's index of consumer confidence fell for the fourth month in a row, from 94.5 in August to 93.3 in September, its lowest reading in ten months. The index's measure of current conditions fell to its lowest level in eight years, although the future expectations index made its first upturn since May. America's buoyant housing market may be cooling: sales of existing homes fell by 1.7% in August.

Germany's Ifo business-confidence index fell for the fourth consecutive month in September, dropping to 88.2 from 88.8 in August, although the reading was better than some analysts had feared. Business confidence in **Italy** improved in September, and industrial output rose by 0.9% in the 12 months to July. Consumer prices in **Germany** rose by 1.1% in the year to September. **Austria's** GDP grew by 0.4% in the year to the second quarter. However, a broader indicator was more gloomy: in the year to July, industrial production in the **euro area** fell by 0.5%.

Britain's government borrowed £2.3 billion (\$3.5 billion) in August, as previously announced spending increases took effect. Public-sector debt stood at 30% of GDP at the end of the month.

Unemployment in **Sweden** fell to 4.1% in August, down from 4.3% a year ago. **Denmark's** broad money growth slowed to 7.0% in the year to August.

Canadian consumer-price inflation in the 12 months to August rose to 2.6%, the highest rate since September 2001, and up from 2.1% in the 12 months to July.

The price of **gold** rose to \$327 an ounce. The price has now risen by 18% this year.

Data on more countries are available to subscribers on www.economist.com

Output, demand and jobs

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production latest	Retail sales (volume) latest		Unemployment % rate	
	1 qtr*	1 year	2002	2003		latest	Q2	latest	year ago
Australia	+ 2.4	+ 3.8 Q2	+ 4.0	+ 3.7	+ 4.3 Q1	+ 6.3	Q2	6.2 Aug	6.8
Austria	na	+ 0.4 Q2	+ 0.9	+ 2.4	+ 2.5 Jun	- 0.2	May	4.2 Jul	3.6
Belgium	+ 0.8	+ 0.3 Q2	+ 1.1	+ 2.7	+ 3.8 Jul	- 4.2	Jun	12.0 Aug†	11.6
Britain	+ 2.4	+ 1.2 Q2	+ 1.7	+ 2.9	- 2.5 Jul	+ 5.0	Aug	5.2 Jul‡	5.1
Canada	+ 4.3	+ 3.2 Q2	+ 3.3	+ 3.4	+ 1.3 Jun	+ 6.3	Jun	7.5 Aug	7.3
Denmark	+ 4.4	+ 2.2 Q2	+ 1.6	+ 2.3	- 1.6 Jul	+ 4.1	Jun	5.1 Aug	5.1
France	+ 2.0	+ 1.0 Q2	+ 1.3	+ 2.6	- 1.7 Jul	+ 3.5	Aug	9.0 Jul††	8.7
Germany	+ 1.1	+ 0.1 Q2	+ 0.6	+ 2.2	- 1.9 Jul	- 1.7	Jul	9.9 Aug§	9.3
Italy	+ 0.9	+ 0.2 Q2	+ 0.8	+ 2.4	+ 0.9 Jul	nil	Jul	9.0 Apr	9.5
Japan	+ 2.6	- 0.7 Q2	- 0.5	+ 1.0	+ 3.3 Jul	- 4.8	Jul	5.4 Jul	5.0
Netherlands	+ 0.5	+ 0.1 Q2	+ 0.9	+ 2.4	- 3.0 Jun	+ 3.2	Jul	2.3 Aug**	2.0
Spain	+ 1.8	+ 2.0 Q2	+ 2.0	+ 2.9	+ 1.8 Jul	na		11.3 Jul	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.8	+ 2.7	- 1.3 Jun	+ 4.7	Jul	4.1 Aug†	4.3
Switzerland	+ 0.4	- 0.4 Q2	+ 0.9	+ 2.2	- 8.8 Q1	+ 1.7	Jul	2.7 Aug†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.5	+ 3.0	+ 0.4 Aug	+ 6.3	Jul	5.7 Aug	4.9
Euro area	+ 1.4	+ 0.6 Q2	+ 1.0	+ 2.4	- 0.5 Jul	- 0.9	Jun	8.3 Jul	8.0

*% change at an annual rate. †Not seasonally adjusted. ‡May-July; claimant count rate 3.1% in Aug. §EU harmonised rate 8.3% in Aug. **Jun-Aug. ††Revised series.

Prices and wages

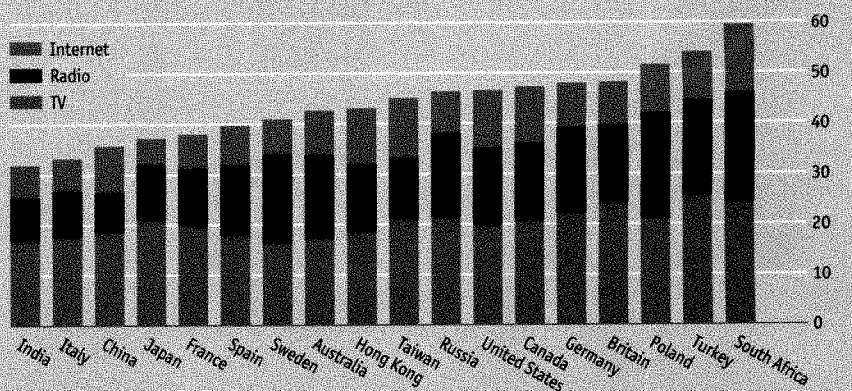
% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2002	2003	latest	year ago	latest	year ago
Australia	+ 2.8 Q2	+ 6.0	+ 2.8	+ 2.5	- 1.1 Q2	+ 5.6	+ 3.7 Q2	+ 4.4
Austria	+ 1.9 Aug	+ 2.5	+ 1.7	+ 1.7	- 0.6 Aug	+ 1.7	+ 2.3 Aug	+ 2.9
Belgium	+ 1.3 Aug	+ 2.7	+ 1.7	+ 1.5	+ 0.8 Aug	- 1.0	+ 2.6 Q2	+ 2.6
Britain	+ 1.4 Aug	+ 2.1	+ 1.9	+ 2.4	+ 0.3 Aug	+ 0.2	+ 4.0 Jul	+ 4.6
Canada	+ 2.6 Aug	+ 2.8	+ 1.8	+ 2.2	- 0.3 Jul	+ 0.8	+ 3.0 Jun	+ 1.5
Denmark	+ 2.3 Aug	+ 2.5	+ 2.3	+ 2.0	- 0.3 Aug	+ 1.5	+ 3.7 Q2	+ 4.7
France	+ 1.8 Aug	+ 1.9	+ 1.8	+ 1.4	- 1.5 Jun	+ 2.3	+ 3.8 Q2	+ 4.2
Germany	+ 1.1 Sep	+ 2.1	+ 1.4	+ 1.2	- 0.5 Aug	+ 1.5	+ 2.1 Jul	+ 1.7
Italy	+ 2.4 Aug	+ 2.8	+ 2.3	+ 1.8	+ 0.1 Jul	+ 1.3	+ 2.2 Jul	+ 2.5
Japan	- 0.8 Jul	- 0.8	- 0.9	- 0.5	- 1.3 Aug	nil	- 5.6 Jul	+ 0.7
Netherlands	+ 3.3 Aug	+ 4.7	+ 3.6	+ 2.4	- 0.4 Jul	+ 2.4	+ 3.0 Jul	+ 5.1
Spain	+ 3.6 Aug	+ 3.7	+ 3.3	+ 2.6	+ 0.5 Aug	+ 1.6	+ 4.0 Q1	+ 3.4
Sweden	+ 2.0 Aug	+ 3.1	+ 2.3	+ 2.0	- 0.8 Jul	+ 2.1	+ 2.9 Jun	+ 2.8
Switzerland	+ 0.5 Aug	+ 1.1	+ 1.0	+ 1.2	- 1.4 Aug	- 0.2	+ 2.5 2001	+ 1.3
United States	+ 1.8 Aug	+ 2.7	+ 1.6	+ 2.2	- 1.6 Aug	+ 2.0	+ 3.1 Aug	+ 4.1
Euro area	+ 2.1 Aug	+ 2.7	+ 2.1	+ 1.6	- 0.6 Jul	+ 2.1	+ 3.3 Q1	+ 2.8

Media habits

According to a study by RoperASW, a consultancy, South Africans say they devote more than eight hours a day to radio, television and recreational use of the Internet. With more than 13 hours a week spent online, they are keener web-surfers than the Americans, Canadians or Taiwanese. Among rich countries, Britain has the most dedicated television watchers, who spend more than 24 hours a week in front of the box.

Average weekly number of hours spent using*:



Source: RoperASW

*People aged 13-65, Spring 2002

Money and interest rates

	Money supply*			Interest rates % p.a. (Sep 25th 2002)						
	% change on year ago			3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds	
	narrow	broad		latest	year ago		latest	year ago		
Australia	- 4.1	+ 9.4	Jul	4.94	4.43	4.80	5.26	5.60	6.28	
Britain	+ 8.6	+ 5.8	Aug	3.91	4.44	3.54	4.41	4.87	5.74	
Canada	+16.2	+ 7.3	Aug	2.83	3.06	3.32	4.92	5.32	6.74	
Denmark	+ 6.3	+ 7.0	Aug	3.40	4.24	3.58	4.50	5.01	6.86	
Japan	+31.5	+ 3.5	Aug	0.01	0.01	0.00	1.17	1.39	1.33	
Sweden	+ 2.2	+ 4.2	Jun	4.15	3.71	4.26	4.83	5.27	4.82	
Switzerland	+12.0	+ 5.8	Aug	0.75	2.25	0.75	2.54	3.22	3.80	
United States	+ 3.2	+ 8.3	Aug	1.75	2.45	1.96	3.75	4.64	6.25†	
Euro area†	+ 7.6	+ 7.1	Jul	3.29	3.65	3.17	4.25	4.75	5.22	

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. ‡Sep 18th. Benchmarks: US 30-year 4.72%, Japan No.242 1.21%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.002%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholm Börsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

Stockmarkets

Market indices

	% change on						
	Sep 25th	2002		one week	record high	Dec 31st 2001	
		high	low			in local currency	in \$ terms
Australia (All Ordinaries)	2,946.6	3,440.0	2,937.8	- 4.0	-14.3	-12.3	- 6.8
Austria (ATX)	1,062.2	1,357.2	1,049.2	- 2.6	-38.9	- 6.9	+ 2.4
Belgium (Bel 20)	1,888.9	2,899.8	1,837.5	- 6.3	-48.7	-32.1	-25.3
Britain (FTSE 100)	3,696.2	5,323.8	3,671.1	- 4.4	-46.7	-29.2	-24.0
Canada (Toronto Composite)	6,165.0	7,958.1	6,068.9	- 2.2	-45.9	-19.8	-19.1
Denmark (KBX)	162.7	233.4	162.7	- 5.7	-46.1	-27.6	-20.3
France (SBF 250)	1,887.3	3,081.9	1,867.0	- 7.4	-57.0	-36.7	-30.4
(CAC 40)	2,785.4	4,688.0	2,742.8	- 7.2	-59.8	-39.8	-33.8
Germany (Xetra DAX)	2,962.5	5,462.6	2,873.2	- 5.2	-63.3	-42.6	-36.9
Italy (BCI)	1,026.4	1,513.0	1,004.3	- 6.8	-53.0	-28.4	-21.3
Japan (Nikkei 225)	9,165.4	11,979.9	9,075.1	- 3.2	-76.4	-13.1	- 7.2
(Topix)	900.9	1,139.4	886.4	- 2.9	-68.8	-12.7	- 6.8
Netherlands (AEX)	300.0	531.2	293.8	- 5.1	-57.2	-40.8	-34.9
Spain (Madrid SE)	577.5	848.1	573.1	- 7.3	-49.6	-29.9	-23.0
Sweden (Affarsvarlden Gen)	133.7	236.8	131.5	- 5.8	-66.6	-42.2	-35.0
Switzerland (Swiss Market)	4,644.6	6,694.1	4,561.4	- 3.5	-44.8	-27.6	-19.7
United States (DJIA)	7,841.8	10,635.3	7,683.1	- 4.0	-33.1	-21.8	-21.8
(S&P 500)	839.7	1,172.5	797.7	- 3.4	-45.0	-26.9	-26.9
(Nasdaq Comp)	1,222.3	2,059.4	1,182.3	- 2.4	-75.8	-37.3	-37.3
Europe (FTSE Eurotop 300) *	821.1	1,279.7	808.6	- 4.9	-51.8	-34.9	-28.4
Euro area (FTSE Eblor 100) *	670.6	1,125.1	657.1	- 6.1	-56.7	-39.7	-33.7
World (MSCI) †	747.1	1,024.4	734.8	- 3.9	-48.4	na	-25.6
World bond market (Salomon) ‡	496.5	504.2	430.3	+ 0.0	- 1.5	na	+12.9

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in \$ terms.

The Economist commodity price index

1995=100

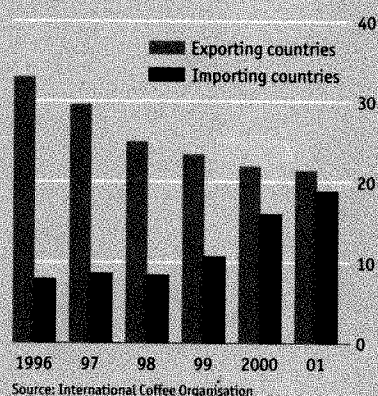
	Sep 17th	Sep 24th*	% change on	
			one month	one year
Dollar index				
All items	75.5	74.6	+ 1.9	+14.9
Food	81.5	80.4	+ 4.3	+19.7
Industrials				
All	67.5	66.8	- 1.7	+ 7.7
Nfa†	69.5	69.6	+ 2.4	+15.5
Metals	65.9	64.5	- 1.6	+ 1.4
Sterling index				
All items	77.6	75.6	+ 0.2	+ 8.4
Euro index				
All items	102.5	100.1	+ 1.8	+ 8.1
Yen index				
All items	98.5	98.0	+ 6.4	+20.7
Gold				
\$ per oz	316.60	326.80	+ 5.1	+12.9
West Texas Intermediate				
\$ per barrel	29.11	30.84	+ 7.0	+41.3

* Provisional. † Non-food agricultural.

Coffee stocks

As coffee-exporting countries have reduced their stocks in recent years, consuming countries have increased theirs. The net result? Global stocks of coffee have hardly changed.

m bags (60 kgs)



Trade, exchange rates and budgets

	Trade balance*, \$bn		Current account				Exchange rate		Currency units					Budget balance % of GDP 2002†
	latest 12 months		\$bn latest 12 mths		The Economist poll % of GDP, forecast 2002		trade-weighted† Sep 25th year ago		per \$ Sep 25th year ago		per £	per euro	per ¥100	
Australia	-	1.3 Jul	-	11.6 Q2	-	3.7 - 3.8	73.2	67.3	1.84	2.04	2.87	1.80	1.50	0.1
Austria	-	1.4 Jun	-	0.9 Jul	-	2.2 - 1.9	na	100.4	1.02	1.09	1.59	-	0.83	-0.3
Belgium	+	14.7 Jul	+	11.8 Mar§	+	5.0 + 5.1	na	99.3	1.02	1.09	1.59	-	0.83	nil
Britain	-	44.9 Jul	-	31.2 Q1	-	2.1 - 1.9	107.1	106.1	0.64	0.68	-	0.63	0.52	-0.8
Canada	+	34.3 Jul	+	12.1 Q2	+	2.1 + 2.2	75.2	76.1	1.58	1.57	2.47	1.55	1.29	1.0
Denmark	+	7.1 Jul	+	3.3 Jul	+	1.9 + 1.8	102.9	103.4	7.59	8.07	11.8	7.43	6.18	2.2
France	+	10.2 Jul	+	27.3 Jul	+	1.7 + 1.6	na	102.0	1.02	1.09	1.59	-	0.83	-2.0
Germany	+	104.5 Jul	+	30.2 Jul	+	1.2 + 1.0	na	99.0	1.02	1.09	1.59	-	0.83	-2.8
Italy	+	9.8 Jun	-	3.2 Jun	-	0.1 nil	na	72.8	1.02	1.09	1.59	-	0.83	-1.4
Japan	+	83.8 Jul	+	110.9 Jul	+	2.9 + 2.9	132.0	141.6	123	118	192	120	-	-8.0
Netherlands	+	25.0 Jul	+	2.7 Q2	+	3.9 + 4.0	na	98.3	1.02	1.09	1.59	-	0.83	0.1
Spain	-	36.4 Jun	-	15.3 Jun	-	2.1 - 1.8	na	74.4	1.02	1.09	1.59	-	0.83	-0.3
Sweden	+	14.6 Aug	+	8.1 Jul	+	3.2 + 3.2	77.4	70.8	9.33	10.8	14.6	9.14	7.60	2.1
Switzerland	+	3.5 Aug	+	22.7 Q2	+	10.0 +10.2	114.4	112.1	1.50	1.60	2.33	1.46	1.22	na
United States	-	438.5 Jul	-	428.8 Q2	-	4.5 - 4.1	114.8	116.6	-	-	1.56	0.98	0.81	-1.0
Euro area	+	83.3 Jul	+	27.5 Jul	+	0.5 + 0.5	81.6	79.7	1.02	1.09	1.59	-	0.83	-1.5

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast. §New series.

Overview

Jitters over the outcome of **Brazil's** presidential election sent the *real* to a record low of 3.78 against the dollar, a fall of almost 40% since the beginning of the year.

Argentina's economic collapse may be bottoming out. In the second quarter, GDP grew by 0.9%. However, economic output was 13.6% lower than a year ago.

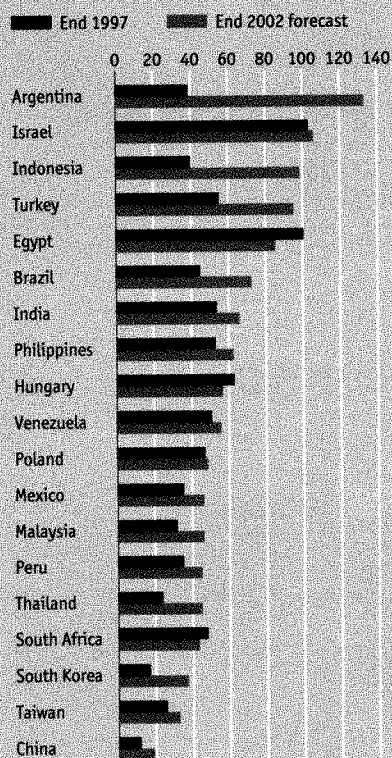
Poland's industrial output fell by 1.1% in the year to August, after rising by 5.7% in the year to July.

Government debt

In most emerging markets governments have taken on more debt over the past five years. As a percentage of GDP, the public debt of Argentina has more than tripled to 133%. By the same measure, the debts of South Korea and Indonesia have both more than doubled.

Are these debts sustainable? The size of the debt to GDP ratio is not the only thing that matters: the pace of GDP growth and real interest rates also determine the burden of debt. By these criteria, the public debts of Indonesia, the Philippines, Mexico, South Africa and South Korea are on a sustainable course. High interest rates faced by Brazil and Turkey, however, suggest that their debts can only get worse.

Government debt as % of GDP



Source: American Express Bank

Economy

	% change on year ago						Latest 12 months, \$bn			Foreign reserves* \$bn, latest		
	GDP		Industrial production		Consumer prices		Trade balance	Current account				
China	+ 8.0	Q2	+12.7	Aug	- 0.7	Aug	+29.1	Aug	+17.4	2001	246.8	Jun
Hong Kong	+ 0.5	Q2	-11.6	Q1	- 3.3	Aug	- 8.2	Jul	+15.7	Q2	112.3	Aug
India	+ 6.4	Q1	+ 6.4	Jul	+ 3.9	Jul	- 5.1	Jul	+ 1.4	Q1	58.3	Aug
Indonesia	+ 3.5	Q2	- 9.4	Q4	+10.6	Aug	+27.3	Jul	+ 6.1	Q1	29.5	Jul
Malaysia	+ 3.8	Q2	+ 6.9	Jul	+ 2.1	Aug	+13.4	Jul	+ 7.0	Q1	32.8	Jul
Philippines	+ 4.5	Q2	+ 6.4	Jul	+ 2.9	Aug	+ 2.8	Jul	+ 6.3	Jun	13.4	Aug
Singapore	+ 3.9	Q2	+15.8	Aug	- 0.4	Aug	+ 6.9	Aug	+17.5	Q2	80.9	Aug
South Korea	+ 6.3	Q2	+ 8.9	Jul	+ 2.4	Aug	+ 9.8	Aug	+ 5.3	Jul	116.5	Aug
Taiwan	+ 3.0	Q2	+ 5.8	Aug	- 0.3	Aug	+18.6	Aug	+24.8	Q2	156.4	Aug
Thailand	+ 5.1	Q2	+ 9.6	Jul	+ 0.3	Aug	+ 3.8	Jul	+ 6.5	Jul	37.0	Jul
Argentina	-13.6	Q2	- 9.2	Aug	+36.5	Aug	+13.4	Jul	nil	Q1	9.0	Jul
Brazil	+ 1.0	Q2	+ 3.3	Jul	+ 7.5	Aug	+ 7.4	Aug	-16.7	Jul	39.1	Jul
Chile	+ 1.7	Q2	+ 8.6	Jul	+ 2.2	Aug	+ 2.4	Aug	- 0.6	Q2	15.0	Jul
Colombia	+ 2.2	Q2	- 1.2	Jun	+ 6.0	Aug	+ 0.5	Jun	- 1.4	Q1	10.6	Jul
Mexico	+ 2.1	Q2	+ 1.9	Jul	+ 5.3	Aug	- 9.0	Aug	-16.3	Q2	46.1	Jul
Peru	+ 3.8	Jul	+ 6.8	Jul	+ 0.1	Aug	+ 0.2	Jul	- 1.0	Q2	9.2	Jul
Venezuela	- 9.9	Q2	-17.1	Jun	+24.0	Aug	+ 8.5	Q2	+ 1.9	Q2	7.6	Jun
Egypt	+ 4.9	2001†	+ 7.8	2001‡	+ 2.7	Jun	- 7.9	Jun	- 0.1	Q1	12.6	May
Israel	- 1.7	Q2	- 1.8	Jul	+ 6.2	Aug	- 6.1	Aug	- 2.3	Q1	24.5	Aug
South Africa	+ 2.2	Q2	+ 7.8	Jul	+11.6	Aug	+ 3.1	Jul	- 0.3	Q2	6.0	Jul
Turkey	+ 2.3	Q1	+12.3	Jul	+40.2	Aug	-10.3	Jun	+ 2.0	Jun	23.2	Jul
Czech Republic	+ 2.5	Q2	+10.8	Jul	+ 0.6	Aug	- 2.3	Aug	- 2.3	Q2	21.6	Aug
Hungary	+ 3.1	Q2	+ 5.1	Jul	+ 4.5	Aug	- 2.5	Jul	- 2.1	Jul	10.3	Jul
Poland	+ 0.8	Q2	- 1.1	Aug	+ 1.2	Aug	-10.4	Jul	- 6.4	Jul	28.3	Aug
Russia	+ 4.1	Q2	+ 3.4	Aug	+15.2	Aug	+42.4	Jul	+28.3	Q2	40.6	Aug

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Financial markets

	Currency units		Interest rates	Stockmarkets	% change on		
	per \$	per £			one week	in local currency	in \$ terms
	Sep 25th	year ago	Sep 25th	Sep 25th			
China	8.28	8.28	12.9	na	1,667.4	+0.2	- 2.6
Hong Kong	7.80	7.80	12.2	1.89	9,124.9	- 3.7	- 19.9
India	48.4	47.9	75.5	5.76	3,021.1	- 1.6	- 7.4
Indonesia	9,000	9,635	14,050	14.27	408.6	- 2.5	+ 4.2
Malaysia	3.80	3.80	5.93	3.20	636.8	- 6.0	- 8.5
Philippines	52.4	51.4	81.8	6.25	1,126.6	- 2.3	- 3.6
Singapore	1.78	1.77	2.78	1.31	1,342.6	- 6.2	- 17.3
South Korea	1,230	1,300	1,920	4.82	658.0	- 6.5	- 5.2
Taiwan	34.9	34.6	54.4	2.10	4,186.0	- 6.6	- 24.6
Thailand	43.4	44.3	67.8	2.00	336.0	- 5.1	+ 10.6
Argentina	3.66	1.00	5.71	32.20	380.1	+0.6	+ 28.7
Brazil	3.75	2.73	5.85	17.90	9,236.0	- 2.8	- 32.0
Chile	745	695	1,164	2.64	4,731.7	- 2.3	- 12.3
Colombia	2,796	2,329	4,365	7.96	1,237.7	+ 2.9	+ 15.6
Mexico	10.27	9.53	16.0	8.60	5,808.4	- 2.5	- 8.8
Peru	3.64	3.48	5.68	16.13	1,149.7	- 1.1	- 2.2
Venezuela	1,463	743	2,283	29.10	7,367.2	- 0.3	+ 12.1
Egypt	4.63	4.25	7.23	7.11	5,275.2	- 0.3	+ 0.1
Israel	4.88	4.36	7.61	6.40	339.5	- 4.3	- 24.0
South Africa	10.6	8.87	16.5	12.55	9,418.2	- 1.7	- 9.8
Turkey	1,650,000	1,552,000	2,575,815	42.00	9,119.2	- 1.5	- 33.8
Czech Republic	31.1	36.9	48.5	2.89	447.9	+0.6	+ 13.5
Hungary	249	279	389	9.69	7,320.1	- 1.6	+ 2.6
Poland	4.15	4.20	6.47	8.02	13,065.3	+0.0	- 6.2
Russia	31.7	29.4	49.4	21.00	343.1†	+ 4.0	+ 36.9
EMF (MSCI)*	1.00	1.00	1.56	na	269.7	- 5.2	na
EMBI+†	1.00	1.00	1.56	na	202.6	- 0.9	na

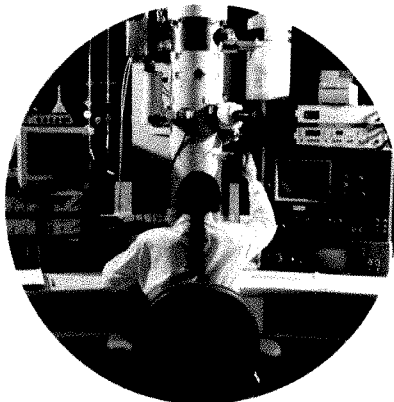
*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In \$ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; UBS Warburg; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; Russian Economic Trends.

Data on more countries are available to subscribers on www.economist.com

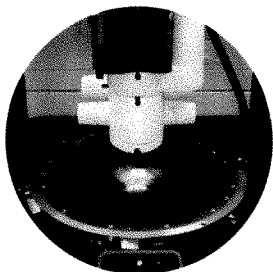
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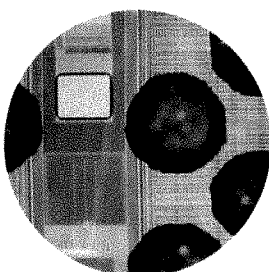


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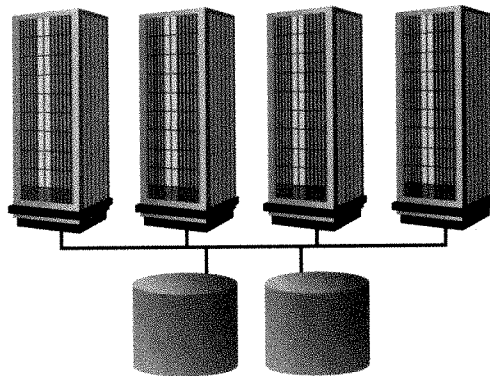


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